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SUPREME COURT, U. S.

In the

Supreme Court of the United States

OCTOBER TERM, 1968

Nos. 914

THE NEW HAVEN RAILROAD TERMS OF SALE AND INCLUSION CASES

In the Matter of

THE NEW YORK, NEW HAVEN & HARTFORD RAILROAD COMPANY,

Debtor.

ON PETITIONS FOR CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

MANUFACTURERS HANOVER TRUST CO., *et al.*,

Appellants,

v.

UNITED STATES OF AMERICA,
INTERSTATE COMMERCE COMMISSION, *et al.*,

Appellees.

APPEALS FROM THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

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F-9459

INTERSTATE COMMERCE COMMISSION

FINANCE DOCKET NO. 21989[1]

PENNSYLVANIA RAILROAD COMPANY–MERGER–NEW YORK CENTRAL RAILROAD COMPANY

Decided November 16, 1967

1. Inclusion in the Pennsylvania New York Central Transportation Company of The New York, New Haven and Hartford Railroad Company, its affiliates and subsidiaries, including the New England Transportation Company, authorized and directed. Just, reasonable, and equitable terms prescribed for loans to The New York, New Haven and Hartford Railroad Company. Prior reports 327 I.C.C. 475, 328 I.C.C. 304, and 330 I.C.C. 328.
2. Authority granted to The Pennsylvania Railroad Company to issue (a) 950,000 shares of its common stock of the par value of $10 per share, and (b) $23-million principal amount of 25-year Divisional First Mortgage Bonds and such additional shares and larger principal amount of bonds as may result from further adjustments.
3. Authority granted to The Pennsylvania Railroad Company to assume obligation and liability in respect of (a) equipment trust obligations guaranteed by The New York, New Haven and Hartford Railroad Company, (b) bonds and certificates of contingent beneficial interest to be issued pursuant to the plan for reorganization of the Boston and Providence Railroad Corporation, and (c) any other securities the New Haven trustees are hereafter authorized to issue, assume, or guarantee under section 20a of the Interstate Commerce Act which The Pennsylvania Railroad Company may be required to assume or guarantee by the terms of their agreement with the New Haven trustees, all in connection with the inclusion approved herein.
4. First step of plan of reorganization of The New York, New Haven and Hartford Railroad Company approved.

Appearances shown in prior reports and *Robert L. King, K. H. Lundmark, Roswell B. Perkins, Francis T. P. Plimpton* and *Morris Raker* for applicants.

[1]Embraced herein are Finance Docket No. 21990, Pennsylvania Railroad Company Stock Issuance; Finance Docket No. 24361, Pennsylvania Railroad Company Securities and Assumption of Obligations; and Finance Docket No. 21669, New York, New Haven & Hartford Railroad Company Reorganization.

William H. Dempsey, Jr., Robert F. Dobbin, Martin J. Flynn, Earle J. Harrington, Daniel J. Kolb, Richard J. Lally, Eugene T. Liipfert, Harold I. Meyerson, John E. O'Brien, Richard Rifkin, Dale Schreiber, and *Francis M. Shea* for intervening railroads.

Herbert F. DeSimone, William J. Lynch, Howard M. Miller, and *Harold M. Mulvey* for States and regulatory agencies.

Paul A. Sweeney for the United States of America, Department of Justice.

Albert X. Bader, Jr., R. Marshall Barnes, Wilkie Bushby, John W. Clarke, John O. Ehrenclou, Paul M. Gartner, Keith B. Hook, Wallace D. Johnson, Paul E. Kern, Walter A. Kernan, Nathan M. Klein, James S. Kleinman, Francis E. Lake, Nathan D. Lobell, Horace J. McAfee, John J. McGraw, Richard K. McLaren, Lester C. Migdal, Lawrence W. Pollack, and *Joseph Schreiber* for other interveners.

SECOND SUPPLEMENTAL REPORT OF THE COMMISSION ON FURTHER HEARING

BY THE COMMISSION:

This report concerns the second major proceeding stemming from the conditions we attached to the approved merger of The New York Central Railroad Company (Central) into The Pennsylvania Railroad Company (Penn), 327 I.C.C. 475 (1966), modified, 328 I.C.C. 304 (1966). In 330 I.C.C. 328 (1967), we rendered a decision, with respect to conditions imposed in appendix G to our report of April 6, 1966 (327 I.C.C. at page 561) and on the issue of capital loss indemnification. Here we are dealing with the inclusion, pursuant to section 5(2)(d) of the Interstate Commerce Act, in the Penn-Central system of The New York, New Haven and Hartford Railroad Company (NH), a debtor in reorganization under section 77 of the Bankruptcy Act, Richard Joyce Smith and William J. Kirk, trustees, "upon such fair and equitable terms as the parties may agree subject to the approval of the Bankruptcy Court and the Commission," 327 I.C.C. at page 553.

Penn, Central, and the NH trustees filed their plan for inclusion and other pleadings on October 27, 1966, and we assigned the following matters for hearing on a consolidated record:

1. In Finance Docket Nos. 21989 and 21990, the joint petition of Penn and Central for approval of a plan to purchase substantially all of the assets and assume certain obligations of NH; and the related supplemental petition of the NH trustees for inclusion in the proposed Penn-Central system;

2. In Finance Docket No. 24361, the application of Penn, in connection with the aforesaid purchase, for authority to issue securities and to assume obligation and liability with respect to securities of others; and

3. In Finance Docket No. 21669, the request of the NH trustees for approval of a plan of reorganization.

We found that due and timely execution of our functions imperatively and unavoidably requires the omission of an examiner's report and recommended order herein and the record has accordingly been certified to us for initial decision.

On August 1, 1967, we directed the NH trustees, Penn, and Central to file an agreement providing for operation of NH by the merged Penn-Central under a lease until ownership of the NH assets could be transferred to Penn-Central, and, in the absence of such an agreement, their respective proposals for terms of a lease. Instead, the NH trustees, on the one hand, and Penn and Central, on the other, filed separate proposals for a loan of $25 million to NH over a 3-year period.

Proposals of Petitioners

Penn, Central, and the NH trustees ask us, pursuant to section 5(2)(d), to approve, as fair and equitable, the purchase of the properties of the NH, after consummation of the merger of Central into Penn, by the Pennsylvania New York Central Transportation Company (Penn-Central) on the terms and conditions contained in an agreement dated April 21, 1966, as amended October 4, 1966. Penn and Central, in addition, request us to authorize the acquisition by Penn-Central, as a result of such purchase, of control through stock ownership or otherwise of other carriers, leases of and rights to operate by contract or otherwise the properties of other carriers, and trackage rights over, and joint ownership in and joint use of, lines owned or operated by other carriers including acquisition by Penn-Central of control through stock owership of New England Transportation Company (NET), a wholly owned motor carrier of property subsidiary of the NH operating under a certificate of public convenience and necessity issued in No. MC-29250.

The agreement provides for the sale of NH's physical assets and investments to Penn-Central after which the NH's operations would be conducted by Penn-Central. With certain exceptions, the NH properties are to be conveyed free and clear of liens and other encumbrances.

Subject to closing date and other adjustments, Penn-Central would pay to the NH trustees for the property (a) 950,000 shares of its capital stock, (b) $8 million in cash, and (c) $23 million in bonds. In addition, Penn-Central would assume NH equipment obligations, a mortgage lien securing not in excess of $3.2-million principal amount of bonds to be issued under the proposed plan of reorganization of the Boston and Providence Railroad Corporation (B&P),[2] an obligation to pay the net proceeds of certain dispositions of B&P properties to holders of certificates of contingent beneficial interest (CCBI's) to be issued under the B&P plan of reorganization,[3] NH's pension costs, and all labor protection costs flowing from the railway employee protective conditions established herein.

Property to be conveyed by the NH trustees to Penn-Central (with certain exceptions) will be subjected to a Penn-Central mortgage to secure that portion of the consideration represented by Penn-Central bonds.

Under section 20a, Penn seeks authority in relation to the above-described transaction with the NH trustees, (1) to issue 950,000 shares of its $10-par value common stock, or such larger or smaller number of shares as may result from operation of the purchase price adjustment and antidilution provisions of the agreement between the parties; (2) to issue $23-million principal amount of 25-year "Divisional First Mortgage Bonds," or such larger or smaller principal amount of bonds as may result from the purchase price adjustment provisions of the purchase agreement; and (3) to assume obligation and liability in respect of (a) designated equipment trust obligations guaranteed by NH, (b) bonds and CCBI's to be issued pursuant to the B&P plan of reorganization and guaranteed or assumed by the NH trustees prior to acquisition of the NH properties by Penn-Central, and (c) any other securities which the latter may be required to assume or guarantee pursuant to the terms of the purchase agreement.

[2] We have approved a plan for reorganization of the B&P, *Boston & P. R. Corp. Reorganization*, 327 I.C.C. 10 (1966), plan approved, *In Re Boston & Providence Railroad Corporation*, 260 F. Supp. 415 (D. Mass. 1966), appeal dismissed *sub nom Boston & Providence Railroad Stockholders Development Group v. Bartlett*, United States Court of Appeals for the First Circuit, No. 6873, March 29, 1967, which provides, among other things, for sale of substantially all of B&P's assets, properties, and franchises to the NH. The trustee of the B&P is to issue certain bonds, and the NH will become the sole obligor on the bonds.

[3] The CCBI's are to be secured by an equitable charge on all of the B&P property acquired by the NH, the NH to become the sole obligor on the CCBI's.

The plan of reorganization submitted by the NH trustees pursuant to section 77 of the Bankruptcy Act envisioned two principal steps, and initially only the first was presented to us for approval. This step provides for NH's inclusion in Penn-Central on the basis of the sale of assets as embodied in the agreement previously described. After consummation of this step, the trustees intended to implement the second step of their plan, which would entail distribution of the assets of the NH estate or the issuance of new NH securities.

The legality of a two-step plan was contested by certain NH bondholder groups. In a decision on May 29, 1967, *In the Matter of The New York, New Haven and Hartford Railroad Company*, 378 F. 2d 635, the United States Court of Appeals for the Second Circuit held that decision on the legality of a two-step plan was premature. As will be discussed later, however, the court did not rule out a two-step plan.

Thereafter, on September 1, 1967, the NH trustees filed amendment No. 2 to the plan for reorganization in which they classify claimants and stockholders, provide for the creation of a reorganized company, and set forth their proposals for treatment of claimants and stockholders.[4] However, the NH trustees request us to make findings required under section 5(2) of the Interstate Commerce Act and not await completion of the reorganization proceeding. A previous amendment to the plan of reorganization, filed on May 2, 1967, provides for rejection of certain leases and executory contracts to which NH is a party, including the lease of the Providence and Worcester Railroad Company (P&W). Subsequently, P&W petitioned for inclusion in Penn-Central.

With regard to interim support of NH, the NH trustees and Penn-Central, as previously indicated, have filed separate loan arrangements rather than provisions for a lease. In general, under the loan arrangements, Penn-Central would make available an aggregate of $25 million to be taken down by NH from time to time as needed over a 3-year period beginning with the consummation of the Penn-Central merger. Every loan takedown would be evidenced by the issuance of trustees' certificates which would

[4]On March 20, 1967, Oscar Gruss & Son, the owner of approximately 10.5-million (14 percent) principal amount of the NH's First and Refunding Mortgage Bonds, filed a petition asking that the NH trustees be directed to supplement their proposal to disclose their intentions with respect to disposition of the proceeds of the sale of the NH properties to Penn-Central and treatment of the claims of the NH creditors. In view of the filing of amendment No. 2 to the plan for reorganization, the Gruss petition will be dismissed as moot.

be on a parity with the NH trustees' certificates presently outstanding in the amount of $12.5 million, and they would represent an administration claim against the NH estate.[5] They would constitute a charge and direct first lien upon all property and earnings of the estate prior in right to the liens, among others, of all mortgages. In addition, the NH trustees propose that Penn-Central absorb NH operating losses, while Penn-Central oppose such provision.

POSITIONS OF THE PARTIES

The NH trustees, Penn and Central support the purchase agreement they reached as presenting fair and equitable terms for inclusion. The NH trustees contend that the record now before us and presented on the first step of the trustees' plan of reorganization is also the complete record for the purpose of the determinations required under section 5(2). They maintain that such determinations are vital to prompt completion of a plan for reorganization of NH. Penn and Central urge that NH's inclusion does not warrant the imposition of any conditions to protect other railroads. They also request that the motor carrier operating rights of NET be transferred to Penn-Central in their present form.

The NH trustees and Penn and Central contend that a lease agreement is not feasible and is unnecessary to secure interim support of NH's operations and that their respective loan proposals satisfactorily achieve that objective. The NH trustees consider it appropriate and in accord with our order of August 1, 1967, to require Penn-Central to absorb at least some portion of NH's operating losses. Penn-Central argue that they should have no responsibility for NH losses until they acquire NH assets and assume authority over NH operations.

The States of Connecticut, New York, and Rhode Island, and the Commonwealth of Massachusetts advocate inclusion of the NH in the Penn-Central system as quickly as possible. Connecticut and New York claim that, if required to do so, the railroads could negotiate a lease agreement. These States ask us to direct the railroads to submit a lease and to provide for a loan arrangement only if required to sustain the NH's operations

[5] On September 25, 1967, the NH trustees filed an application in Finance Docket No. 24756 for authority to issue the trustees' certificates. An order granting appropriate authority is being issued concurrently with the service of this report and order.

until a lease becomes effective. Rhode Island and Massachusetts prefer a lease but support the NH trustees' proposal in the present context of the case.

NH security holders and trustees under mortgage bond indentures argue that the sale price for the NH properties is grossly inadequate.[6] John Ehrenclou, an individual security holder, takes the position that NH should not be imposed on Penn-Central and that there are other possible solutions to the NH problem. Chase Manhattan Bank (Chase), trustee under NH's General Income Mortgage Bond Indenture, joins in the NH trustees' request that the Commission now find "equitable terms" for inclusion under section 5(2)(d). The First Mortgage 4 Percent Bondholders Committee (Committee) and Oscar Gruss & Son (Gruss)[7] assert that we should not and cannot properly make section 5 findings independently of the complete plan of reorganization.

Most of the creditor groups urge an immediate takeover of NH's operations by Penn-Central under a lease and oppose a loan arrangement. The Committee urges that summary provisions submitted by Manufacturers Hanover Trust Company (Manufacturers) in its brief can be used as the basis for a lease. Gruss has presented similar provisions, differing principally with respect to the amount of rental to be paid by Penn-Central and clearly permitting Penn-Central to effect operating economies. It also declares that, to the extent our order of September 12, 1967, permits consummation of the Penn-Central merger pending determination of this matter, the order constitutes a prejudgment of the issue and the recital should be rescinded. Chase claims that the public hearing on the issuance of NH securities was without legal foundation because the NH trustees have no authority to issue trustees' certificates in connection with a loan agreement. It also contends that the loan proposals do not afford a real solution for NH cash problems because the proposals are bottomed on the Penn-Central merger and it is doubtful that the merger will be consummated in time to help NH. Chase maintains that effective help can be secured through discontinuance of NH passenger service unless public authorities agree to pay an adequate subsidy. If a takeover by lease is not required, some of the creditor groups claim that, after the Penn-Central merger, NH is entitled to protection against potential diversion of traffic until it is included in Penn-Central.

[6]See appendix A for a table of the NH's funded debt.

[7]See footnote 4.

Boston & Maine Corpertation (B&M), The Delaware and Hudson Railroad Corporation (D&H), Erie-Lackawanna Railroad Company (EL), the trustees of the Central Railroad Company of New Jersey (CNJ), Reading Company (Reading), and Western Maryland Railway Company (WM) seek protection because of the inclusion of NH in Penn-Central. The last four railroads request imposition of conditions which would remain in effect even if they should be included in a major Eastern railway system. EL, CNJ, and Reading also ask protection in connection with interim support of NH's operations by Penn-Central.

P&W requests us to disapprove the amendment to the NH trustees' plan of reorganization which rejects the NH lease with P&W and asks that it be included in Penn-Central as part of NH under the terms and conditions of the existing lease.[8]

Boston & Providence Railroad Development Group (B&P Group) asks that the B&P be included in the Penn-Central system directly rather than only to the extent its properties are presently operated by NH. It also supports an immediate takeover of NH or B&P by Penn-Central.

Milton J. Shapp, a Penn stockholder and a resident of Pennsylvania, declares that the merger of Central into Penn must be reevaluated in the light of evidence showing the adverse impact of the NH inclusion on anticipated Penn-Central merger savings. Furthermore, he claims that, in view of the Supreme Court's decision delaying consummation of the Penn-Central merger, *Baltimore & Ohio* v. *United States*, 386 U.S. 372 (1967), and the May 29, 1967, Court of Appeals decision, *supra*, concerning the NH trustees' two-step plan of reorganization, there does not presently exist any ground for finding that execution of our functions imperatively and unavoidably requires the omission of an examiner's report. Shapp contends the record does not establish that the NH's situation is critical, and he is against any Penn-Central support for the NH operations through lease, loan, or otherwise.

DESCRIPTION OF NH

The NH, a class I railroad operating in New York, Connecticut, Rhode Island, and Massachusetts, has been in reorganization

[8]By letter dated July 25, 1967, P&W argues that the portion of the Penn-Central reply brief which deals with P&W should have been contained in Penn-Central's initial brief. P&W asks us not to devote any attention to this portion of the Penn-Central reply brief or else grant P&W an opportunity to respond thereto. We do not find the contents of Penn-Central's brief improper reply material and deny P&W's request.

since July 1961. The nature and scope of its operations, as well as the financial deterioration which has occurred since 1954, are detailed in the hearing examiner's report herein of March 29, 1965, page 321 *et seq.*, and in *New York, N.H. & H. R. Co. Discontinuance of Trains*, 327 I.C.C. 151, 163 *et seq.* (1966). Reiteration of these matters is unnecessary. For summaries of financial data, see appendixes B through D.

Of particular significance at this time is NH's cash position. Between the beginning of their trusteeship and the end of 1966, the NH trustees were able to hold the attrition in NH's cash within manageable limits. The cash balance of NH at December 31, 1966, was $9.8 million including proceeds from trustees' certificates except for $1.5 million reserved for payment of Federal income and railroad retirement taxes. By August 31, 1967, this cash balance had fallen to $4.5 million. It is estimated that by the end of 1967 the cash balance will have further decreased to $3.1 million and that by the end of February 1968 it will only be $850,000. In contrast, a week's payroll plus expenditures for materials and supplies requires $1.75 million in cash.

It is obvious, therefore, that the time is fast approaching when NH's capability to conduct day-to-day operations will be materially imperiled. These circumstances accent the need for immediate action if NH's services are to be maintained.

Scope of this Report

The NH trustees urge that we do not await the hearing on amendment No. 2 to their plan for reorganization of the NH and resolution of the issues involved therewith,[9] but that we proceed to a prompt determination of terms and conditions for inclusion of NH in Penn-Central under section 5(2) of the Interstate Commerce Act. They contend that there are unique reasons why a determination under section 5(2)(d) should be made at this time and point to a petition filed by the Committee and pending before the reorganization court seeking to have NH liquidated. The NH trustees maintain that a determination of terms for inclusion of NH which embodies our valuation will provide the necessary guide for consideration of the issues raised by the Committee's petition. Furthermore, the NH trustees claim that if there be any question of different standards with regard to the "equitable

[9] By order of October 5, 1967, the matter has been set down for hearing to start on November 29, 1967.

terms" language of section 5(2)(d) of the Interstate Commerce Act and the standard of "fair and equitable" in section 77(e) of the Bankruptcy Act, we may properly adopt the latter criterion for purposes of determining equitable terms under section 5(2)(d).

Chase supports the NH trustees on different grounds. Chase argues that it is useless for the NH trustees to file a supplemental plan allocating among creditors a consideration with which such creditors are in total disagreement. Chase suggests that once we have made a preliminary finding of value, adopting its contentions and requiring payment of a greatly increased consideration for the NH assets, a distribution of the consideration among NH creditors would have substance and meaning.

The Committee and Gruss oppose findings under section 5(2)(d) separate from findings on a complete plan of reorganization.

The Committee contends that a price for NH established by the Commission as equitable under section 5(2)(d) may be one indication of value for purposes of section 77(e), but it is not the only basis for determining value under that section. The Committee's position is, therefore, that little will be gained from an abstract announcement of equitable terms under section 5(2)(d), but that, to the contrary, findings under section 5(2)(d) would confuse the question of valuation as well as the entire reorganization.

Gruss avers that we must consider the creditors' claims, in the order of priority, and know what, if anything, is provided in satisfaction thereof, before we can arrive at equitable terms. A valuation made under section 5(2)(d) before completion of the record required by section 77(d) of the Bankruptcy Act would, according to Gruss, almost certainly set in motion review proceedings before two different courts, one to deal with the section 5(2)(d) findings outside the court review provided in section 77, and the other under section 77 before the reorganization court, a matter we do not pass on.

We shall grant the request of the NH trustees. At the heart of the controversy over whether to make section 5(2)(d) findings on the present record are the valuation of the NH properties and the consideration that should be paid for them. We are convinced that further delay is not justified, and that findings are warranted which would both make possible an expedited NH inclusion and fully satisfy the equity requirements of the Bankruptcy statute. Such findings are permitted by the law, fully supported by the record and urgently compelled by the exigencies of the NH's plight.

Our prime purpose in requiring inclusion of NH in the merged Penn-Central system is to assure continuity of NH service (which we have found essential to the public) as an integrated part of the Penn-Central system and under the system's management. In recognition of NH's rapid and persistent financial deterioration, a 6-month period was set for submission by the parties of a plan to effectuate the inclusion.

It was found that the dire financial condition of NH, for which neither Penn nor Central could be held responsible, rendered NH incapable of withstanding competition from the merged system, or from any significantly increased rail competition, and that finding has been amply confirmed by the erosion of NH's position to a point where a shutdown of operations is imminent for lack of operating funds.

To place the NH problem in perspective, we first note that at the time of our first report in these proceedings the public interest considerations affecting the entire eastern district, and even territory beyond, justified the approval of the Penn-Central merger despite the weak position of NH. Certainly, the plight of that company was not reason enough to deny the public in general and the shipping public in particular the many economic and transportation benefits the Penn-Central merger will produce. Neither do we consider the private interests of NH bondholders in securing the maximum possible return on their accounts as now justifying a further withholding of the merger benefits from the public.

A section 5(2)(d) decision will satisfy a legal preliminary to NH inclusion without delay once the Penn-Central merger is consummated. On the other hand, delaying such a decision, as advocated by the Committee and Gruss, until NH's reorganization is completed would most assuredly preclude a timely rescue of the NH as an operational common carrier; for there could be no hope that Penn-Central would be authorized in time to assume operation of NH before the latter exhausts its funds and shuts down.

The choice is clear: either the public at large is forced to stand in the wings awaiting progress in transportation while the NH creditors haggle on stage over the wasting corpus of the NH estate, or, on the other hand, the overall objectives of the law are served, with the broad public interest brought into the scene in the form of improved service through a consummated Penn-Central merger including an operational NH, while the

NH creditors are freed to litigate at will the distribution of their estate.

It is true that a carrier proposal approved under section 5(2) may, in a particular case, be only one of many possible just and reasonable plans which might be advanced for the purpose sought to be achieved. This case is different. Here both the inclusion transaction and the terms for it are pursuant to a Commission prescription made in particular reference to the NH's posture; and with the trustees, we believe that any terms prescribed under section 5(2) to meet the unique and critical situation of this case should be devised as well to satisfy section 77 of the Bankruptcy Act.

Nothing in the law or in the facts of this case indicate that just and reasonable terms for inclusion of NH under section 5(2)(d) would be incompatible with the findings of fairness and equity required by section 77. All persons interested in the reorganization of NH have been afforded every opportunity to furnish evidence as to NH's value and, in fact, because hearings were conducted in contemplation of a two-step reorganization plan, both creditors and trustees have addressed evidence and argument toward that end. In the light of that evidence, the terms we are prescribing under section 5(2)(d) have been specifically devised to satisfy the requirements of section 77. Section 77 of the Bankruptcy Act and its application here will be discussed in more detail later in connection with the NH trustees' request for findings on valuation under section 77(e).

Public interest requires prompt consummation of the Penn-Central merger and continuity of NH service as well as the reorganization of NH. We are attempting to further the public interest by expediting these proceedings to the extent possible within the confines of due process. The danger that NH cannot long continue its railroad operations is very real. A failure on our part to make, at this time, the findings and arrive at the conclusions which the circumstances demand and the record supports, would gravely affect the interests of the public and would be a disservice to the parties. Inasmuch as the record is also complete with respect to Penn's section 20a application, and such application is a concomitant of the section 5 petitions, we shall also set forth in this report our findings under section 20a.

Finally, we shall dispose of the matter of support for NH for the interim period until its assets can be conveyed to Penn-Central.

PRELIMINARY MATTERS

Examiner's report.– Shapp's contention that there cannot now exist any ground for omitting the hearing examiner's report herein is without merit. A paramount consideration in these proceedings is the continuation of NH's essential service. As previously stated, the record demonstrates that such service is in jeopardy because of the serious attrition of NH's cash resources. The findings and conclusions made herein and the action resulting therefrom are designed to meet this problem. To await an examiner's report and the procedures that must follow, would postpone unduly the resolution of the matter.

Reevaluation of Penn-Central merger.– Shapp also maintains that the Penn-Central merger must now be reassessed in light of the evidence of record showing the adverse impact of NH inclusion on anticipated merger savings. He refers to a $220-million burden to purchase the NH and NH operating deficit of $8.5 million per year. This contention also lacks substance.

We were aware of the NH's deficit operations and the extent thereof at the time we approved the Penn-Central merger on the condition that NH be included in the new system.[10] Therefore, the evidence of record adduced at the most recent hearings concerning NH's deficit operations does not present a new circumstance for consideration.

As regards the cost to Penn-Central of acquiring the NH, the specific purpose of this proceeding is to establish fair and equitable terms for the purchase. We have found the Penn-Central merger to be consistent with the public interest subject to the condition, among others, that NH be included in the resultant system under fair and equitable terms. Consummation of the merger prior to the NH inclusion would bind the merger applicants to the inclusion terms thereafter determined by us. But within the contemplation of the prior (merger) decision and of the applicable law, we would not, of course, prescribe inclusion terms that would render the entire transaction inconsistent with the public interest nor terms that would not be fair and equitable to all parties, including Penn-Central and the public, under the circumstances of this case.

[10] These matters were fully developed in the record at the earlier hearings herein and at the hearings giving rise to our report in the train discontinuance case, which report was released concurrently with our original decision approving the Penn-Central merger.

B&P.– The request of the B&P Group for inclusion of the B&P in Penn-Central in B&P's own right was denied in our report, 327 I.C.C. at pages 323-324. No different result is sustained by the record made at this further hearing.

Alternatives to NH's inclusion in Penn-Central.– John O. Ehrenclou, a holder of NH securities, contends that NH's inclusion in Penn-Central is not the only possible solution for NH's problems. He refers to the "Priblic" plan of reorganization and also to the possibility of a State authority operating the NH's commuter service. Ehrenclou's contentions lack substance. A request for hearing on the "Priblic" plan has already been denied because that plan on its face is not a feasible means of reorganizing the NH. Nor does the evidence in this record firmly establish that the NH could be operated at a profit if it were relieved of its responsibilities with respect to commuter service.

VALUE OF THE NEW HAVEN

Criteria.– The valuation of railroad properties involves the application of informed judgment to many factors incapable of precise measurement. No mathematical formula is available; no scientific accuracy can be expected. *Group of Investors* v. *Milwaukee R. Co.*, 318 U.S. 523, 565 (1943); *Nashville, C. & St. L. Ry.* v. *Browning*, 310 U.S. 362, 370 (1940); *Chicago, B. & Q. Ry. Co.* v. *Babcock*, 204 U.S. 585, 598 (1907). Earnings have been a primary criterion of value in a number of reorganization cases. However, other criteria are not to be disregarded. *Investors* v. *Milwaukee*, *supra*, 318 U.S. at pages 540-541.

In the *N&W Inclusion* case (*Norfolk & W. Ry. Co. and New York, Chicago & St. Louis*, 330 I.C.C. 780; 331 I.C.C. 22), we set out in detail the general principles of valuation under section 5(2)(d). We noted that we do "not usually formulate the fair exchange ratios between mutually negotiating parties but merely ascertain from the record whether the agreed upon ratios are fair and reasonable." (330 I.C.C. at page 800) We went on to say that where a transaction is bargained at arm's length each side is presumably capable of determining its own best interest, and our primary function is to discover whether the transaction will be in the public interest. We declared that, in contrast, inclusion under section 5(2)(d) can involve "nonconsent and inequality of bargaining power" (330 I.C.C. at page 801), and that the proceed-

ing before us "replaces the bargaining session" (330 I.C.C. at page 800).

The financial terms arrived at here under section 5(2)(d) will also constitute the comparable terms under section 77 of the Bankruptcy Act. And under that act the Commission must exercise its independent judgment notwithstanding the fact that an agreement has been reached. Accordingly, while the agreement carries some probative force as to the values of the properties involved, it is by no means controlling. We look upon the fact of the agreement as an indication that the NH trustees did have a degree of bargaining power and that the negotiated price, therefore, could well be above the minimum to which the creditors are entitled.

In the negotiations leading to the agreement, asset value was the primary determinant rather than earning power; for, as we explain later, the NH has long been dry of earning power. Further, the evidence introduced at the further hearing herein was directed largely toward showing asset values upon an assumed liquidation. This approach had the appearance of satisfying the standards of section 77(b) of the Bankruptcy Act, which, as pertinent, provides that "a plan of reorganization within the meaning of this section *** (5) shall provide adequate means for execution of the plan, which may include *** the sale of all or any part of the property of the debtor either subject to or free from any lien at not less than a fair upset price.***".

We do not look upon liquidation value as necessarily being the equivalent of "a fair upset price." A liquidation contemplates a dismantling of the railroad and, therefore, an abandonment of the railroad's operations—eventualities hardly likely, in view of our findings in the prior reports herein that the services of the NH are essential. As the Supreme Court pointed out in *Ecker* v. *Western Pacific R. Corp.*, 318 U.S. 448 (1943), in the reorganization contemplated by section 77, "*** the public interest, as distinguished from private, bulks large ***" (page 468) and "the interest of the public in an adequate transportation service must receive consideration" (page 482). See also *First Nat'l. Bank* v. *Fiershem*, 290 U.S. 504 (1954). Moreover, one of the purposes of this special rail reorganization statute was to make possible the continuity of rail service. The act drew upon the theory of debtor rehabilitation by adjustment of creditors' claims. Such treatment was essential for embarrassed railroads, since ordinary bankruptcy liquidation or judicial sales were impossible

because of the size of their indebtedness and the paucity of buyers to continue operations of a railroad in place. See *Ecker* case, *supra*, at page 469.

In the circumstances of the NH, a fair upset price should be geared to the requirement that very large segments of the railroad, though probably not all of it, would have to be maintained in operation. Consideration should be given to the possibility that to effect the continuity of service, public agencies might have to purchase or operate the needed facilities. And in that case, the pricing would be lower than a complete liquidation could produce.

The preservation of facilities in place for continuing the needed service also makes it appropriate for us to consider the going concern value of the railroad. In such an analysis the NH's huge passenger deficit would have the effect of depressing the valuation. These various considerations point up the difficulty of arriving at specific dollar values for the NH as a whole or for its individual items of equipment and facilities. Since the evidence as to the value of the NH properties has been based primarily on an assumed liquidation, we conclude that, if the consideration to be paid is the equivalent of the liquidation value, it will exceed the fair upset price contemplated by section 77(b)(5).

The NH has suffered deficits in net railway operating income, in income available for fixed charges, and in net income each year since 1959. Its net deficits since 1959 have ranged from $4.7 million in 1960 to a high of $20 million in 1961. This net deficit was $11.3 million in 1966, and more than $106 million in the 9 years ending with 1966. Past experience, therefore, furnishes no basis for valuing NH from an earnings standpoint, except to emphasize the chronic deficit character of the operation which is likely to persist and render the operation a burden rather than an income producer.

As regards the future, Penn and Central claim that NH is incapable of being transformed into a profitable concern. The NH trustees and certain bondholder groups have presented evidence with regard to the financial results of NH as a freight-only railroad. Indeed, one of the bondholder groups argues that NH is entitled to be fully subsidized if it should be required to continue passenger operations and that it must be valued in such light.

NH and predecessors have been conducting passenger and freight operations for over 100 years. We have required that all the NH operations, passenger and freight, be included in

Penn-Central. Consequently, to assume a freight-only operation ignores the realities of the situation. Furthermore, there is no legal ground for the proposition that NH is entitled to be fully subsidized if it is required to continue passenger operations. The record reveals no such commitment by any governmental authority. The NH bondholders were, or should have been, aware when they invested in NH that they bore the financial risk for all of NH's operations. Nevertheless, to the extent the evidence of freight-only operations provides some basis of value, we have considered it. Moreover, it is undisputed that as a passenger operation only NH would sustain substantial deficits.

The NH trustees believe that, at best, NH as an independent freight-only railroad would no more than break even for the foreseeable future. Including the freight-only operation in the Penn-Central system, they estimate $12 million of income available for fixed charges as the ultimate possibility.

A study made for certain of the bondholder groups shows that a freight-only service by the NH as an independent railroad would earn $7 million in income available for fixed charges based on 1965 data. In addition, it was estimated that merger of an NH freight-only railroad into the Penn-Central system would yield annual savings of $5.5 million. Although the freight-only study is of dubious value inasmuch as it was not projected beyond 1965, it is noteworthy that the total annual income available for fixed charges estimated therein, $12.5 million, is in line with the estimate of the NH trustees.[11]

If the $12.5-million figure were capitalized at 8 percent, the percentage factor employed by an NH trustee and the lowest such rate in the record, a value of $156 million would be indicated. On the other hand, Penn-Central claims that, assuming earnings for the NH, a reasonable capitalization rate to apply would be not less than 13 percent and probably substantially in excess of that rate. Application of a 13-percent rate would produce a value of $96 million.

Asset values.–Complete studies have been presented by both the NH trustees and the Penn-Central relating to the liquidation value of the NH assets.[12] The NH study is based on the assets held on

[11] Assuming all savings are credited to the NH.

[12] On brief, the NH trustees renew their objection to receipt of the Penn-Central liquidation value study in evidence. The objection was made on the ground that, inasmuch as there was an agreement between the NH trustees and Penn and Central and the Penn-Central valuation did not come into the negotiations, the NH trustees did not want to be placed in the position of cross-examining on the Penn-Central liquidation study and thereby cast doubt on the agreement.
(footnote continued on next page)

December 31, 1965, and the Penn-Central study uses a date 1 year later. Although they accept the study of the NH trustees in many respects, the creditor groups presented evidence pertaining to liquidation value of certain assets.

A large difference between the liquidation values of the assets in the respective studies exists even though each of the parties made comparable studies of the same units and classes of NH assets. Material differences respecting classes of assets appear in the prices and values of land, rails, ties, other track material, freight and passenger cars, and other classes of operating property. Important differences appear in the liquidation values of investment in stocks and other investments, other assets, and in deductions for expenses of liquidating assets and discounting of future selling price to present worth of assets. The liquidation values of the various classes of assets reflected in the NH trustees' studies are considerably higher than liquidation values reflected in the Penn-Central studies, as indicated later. Comparison with and discussion of valuation figures constructed by creditors also appear later in this report.

The NH study was made over a period of approximately 9 months by persons familiar with the NH, the area in which it operates, and the nature and condition of its properties. The Penn-Central study, on the other hand, was made in less than 2 months by persons less familiar with NH, the area in which it operates, and the nature and condition of its properties. Penn-Central urge that the present liquidation value of NH assets is only $51 million, but claim the cost of purchasing the assets is in the neighborhood of $200 million. Either Penn-Central are overpaying or the liquidation value of the NH is greater than they contend. We are satisfied that the latter is the case.

The gross values of groups of assets in a liquidation, as shown by the NH trustees and Penn-Central, before making any deduction for expenses of liquidating assets and for discounting of proceeds to present worth, are:

(footnote 12 continued)

The objection in no way supports rejection of the evidence. It is our duty to determine the value of the NH properties on the basis of all the evidence pertaining thereto, not merely the agreement and supporting evidence. There is no question that Penn-Central's evidence is material and relevant. Accordingly, we sustain the examiner's overruling the objection to its receipt.

Asset groups and ICC account number	Gross liquidation values of assets		
	NH trustees	Penn-Central	Differences
	000	*000*	*000*
Current assets (701-715)	$15,435	$16,769	$1,669
Special funds (716-717)	13,199	12,233	966
Investments (721-725)	20,889	15,873	5,016
Properties (731-735)	173,441	102,622	70,819
Other assets (741-745)[1]	4,825	3,324	1,499
Total	230,290	150,321	79,969

[1]Does not include amounts recorded in ICC account No. 737 for properties in Grand Central Terminal area.

The amounts shown for total gross value of assets include certain current and other assets which are not to be conveyed under the purchase agreement. The amounts so included are $32,379,000 in the NH trustees' study, and $29,888,000 in Penn-Central's. Such amounts should be eliminated to permit meaningful assessment of the consideration. This reduces the total gross value for the trustees' study to $197,911,000, and for the Penn-Central study to $120,433,000.

Both the NH trustees and Penn-Central recognize the validity of deductions from gross liquidation value for expenses of liquidating assets over a period of time and discounting of proceeds to be realized at a later date to their present worth. The studies for Penn-Central were prepared on a basis of a 10-year period for total liquidation; the NH trustees' studies were prepared on a basis of 6-year and 10-year periods for liquidation expenses but for only a 6-year period for discounting to present worth. The net liquidation value of assets, after deducting liquidation expenses and discounting to present worth is shown by the respective studies as:

	Net liquidation values of assets		
	NH trustees		Penn-Central
	6-year liquidation	10-year liquidation	10-year liquidation
	000	*000*	*000*
Gross value of assets[1]	$230,290	$230,290	$150,321
Liquidation expenses	-59,480	-76,847	-62,171
	170,810	153,443	88,150
Discount (to present worth)	-17,563	-17,563	-7,147
Net value after deducting liquidation expenses and discounting to present worth[1]	153,247	[2]135,880	81,003

[1]Does not include properties in Grand Central Terminal area.

[2]Trustees do not show present worth with discounting on 10-year basis. Their witness testified it would be a larger discount than on a 6-year basis, which is $17,563,000. Applying this amount to the 10-year liquidation figures produces $135,880,000 as here shown.

After eliminating the current and other assets not to be conveyed to Penn-Central, the above net values are reduced to $120,868,000, $103,501,000, and $51,115,000 for the NH trustees' 6- and 10-year studies and the Penn-Central study, respectively.

Liquidation expenses.—As indicated, liquidation expenses applicable to an assumed liquidation of NH aggregate substantial sums whether computed over a 6-year or a 10-year period of time. Liquidation expenses include expenses of the real estate department in selling and disposing of land; discounting the current market value of the land on the assumption that a certain portion of the land would remain unsold at the commencement of the final year of liquidation and full market value would not be realized; unpaid real estate taxes and interest thereon that would have to be paid before sale in order to realize full market value; and the cost of selling and disposing of property other than real estate and taxes on such property. These expenses are summarized below.

	Liquidation expenses of assets		
	NH trustees		Penn-Central
	6-year liquidation	10-year liquidation	10-year liquidation
	000	*000*	*000*
Real estate department	$15,971	$18,618	$22,922
Discount for final year of sale of (unsold) real estate	8,178	21,319	4,538
Unpaid real estate taxes and interest	17,449	17,449	16,973
Cost of liquidating property other than real estate	15,648	17,226	15,648
Taxes on property, other than real estate	2,235	2,235	2,091
Total	59,481	76,847	62,172

The NH study of the estimated expenses, stated, in effect, that the assumption that the liquidation could be fully accomplished within 6 years is optimistic. For this reason, liquidation expenses were also computed on a 10-year basis.

Penn-Central assumed a 10-year requirement for liquidation in estimating liquidation expenses. They used NH trustees' estimates for most nonreal estate liquidation expenses, and also made computations on a 10-year basis on their own estimates.

The vice president of a real estate firm made a study of the liquidation value of the real estate for the NH trustees. He expressed the opinion that liquidation of the major portion of the real estate would require at least 5 years with an additional year for disposal of the least salable property and that the estimate of 6-year disposal is low.[13]

As regards a 6-year versus a 10-year period for liquidation, the longer the period taken for liquidation, the greater would be the administration expenses of the real estate department and the management expenses in selling the property, as well as additional taxes on the property during the longer period. Approximately 60 percent of the total liquidation value of NH property is in real estate. In an assumed liquidation of NH, it is fair to conclude that sale of the assets, including real estate, would be made as soon as practicable and we believe that the bulk of the liquidation could be completed within a period of 6 years.

Chase contends that the unpaid real estate taxes and interest should be eliminated from liquidation expenses because the NH property is to be conveyed free and clear of virtually all liens and other encumbrances. This is based on the assumption that the NH trustees could make arrangements with the taxing authorities for satisfaction of such liens.

Amendment No. 2 to the NH trustees' plan for reorganization indicates that unpaid real estate taxes will be paid in full by issuance and delivery of income notes of the reorganized company. Accordingly, we cannot assume that NH will be able to convey its properties without payment of the taxes. The amounts due were $16,072,565 in taxes as of December 31, 1965, and $1,376,580 in unpaid interest thereon.

The NH trustees propose full payment of the interest accrued to July 7, 1961, through the issuance and delivery of income notes but to make no payment on interest commencing that date. The record shows the amount of prebankruptcy interest to be $126,733, and the postbankruptcy interest $1,249,847. The latter amount will be deleted from liquidation expenses.

[13] The Committee and Manufacturers claim no deduction should be made for liquidation expenses. This position is utterly without merit.

In discounting the anticipated liquidation proceeds to present worth, the NH trustees used a discount rate of 6 percent based on a 6-year liquidation period. Penn-Central considered a 6-percent rate too low in view of the risks and uncertainties involved in the liquidation and applied a rate of 7 percent based on a 10-year period.

The record supports the 6-percent rate applied by the NH trustees. The valuation of the assets themselves are sufficiently conservative so that, when weighed with other pertinent considerations, they offset the factors which moved Penn-Central to urge a higher rate.

Liquidation value of classes of assets—in general.—As already indicated, the gross liquidation value of the total NH assets is $79,969,000 more under the NH trustees' studies than under the Penn-Central studies. Of this amount, approximately $1.7 million is in current assets; $966,000 in special funds; $5 million in stock and other investments; $70.8 million in land and other physical property; and $1.5 million in miscellaneous assets and deferred items.[14] Current assets, other than material and supplies, are to be retained by the NH trustees pursuant to section 4 of the purchase agreement; however, any claim for rental based on the excess of income derived from Grand Central Terminal property is transferred to Penn-Central pursuant to section 3.4 of the agreement.

Valuation of current assets (accounts Nos. 701-713).—The NH trustees' valuation of current assets is $1.7 million in excess of the Penn-Central valuation. Part of this difference is due to the 1-year earlier valuation date used by the trustees. However, the only substantial difference is due to elimination from total assets by Penn-Central of uncollected rental from the Grand Central Terminal area properties. This matter will be discussed in detail later.

Valuation of special funds (accounts Nos. 716-717).—Special funds held in escrow and other deposits consist principally of proceeds from the sale of property, proceeds from trustees' certificates and other assets to be retained by the NH trustees.

The trustees' valuation of special funds is $966,000 in excess of Penn-Central's valuation. However, the trustees' valuation was

[14] The principal amount of current assets (other than material and supplies) and much of the assets classified under "other assets and deferred charges" (excludes properties and investments) are not to be conveyed to Penn-Central pursuant to section 3 of the purchase agreement. Certain current accounts receivable and other working assets are to be transferred to Penn-Central, which will also assume certain current liabilities under section 7 of the agreement.

made 1 year earlier, before withdrawal of a substantial sum held in escrow from proceeds of sale of property.

Valuation of investments (accounts Nos. 721–723).—The NH trustees' valuation of investments is $5 million in excess of the Penn-Central valuation. This excess consists principally of differences placed on the value of stock and notes of two affiliated companies.

Name of Company	Value of investments	
	Trustees	Penn-Central
Boston Terminal Corporation (book value $1,140,625)	$1,856,300	$1,109,900
Providence Produce Warehouse Co. stock and notes (book value $6,976,403)	8,516,400	4,586,600
	10,372,700	5,696,500
Excess of trustees' valuation	4,676,200	

The Boston Terminal Corporation's stockholder equity was estimated by the NH trustees at $2,651,860, excluding the value of a mortgage note of the Boston Redevelopment Authority. NH's share (70 percent) amounts to $1,856,300, which is the value used by the trustees. Penn-Central, on the other hand, placed a value of $1,585,500 on the stockholders' equity and assigned 70 percent of that amount, or $1,109,900, as NH's interest.

The Providence Produce Warehouse Co. stock is owned wholly by the NH. The NH trustees valued the real estate owned by that company at $6,500,000 and other assets at $2,016,400, for a total of $8,516,400. Penn-Central valued the real estate at $3,060,000 and other assets at $1,526,000, for a total of $4,586,600. During 1965 no dividends or interest were received on the stock or notes of this company, but in 1966 interest on the notes amounting to $1,175,000 was included in NH's income. Also, during 1966 there were four sales of property totaling $194,100 and the warehouse company received $292,460 as initial payments from other completed sales.

Because of the NH trustees' greater familiarity with the subject properties, we believe their estimates to be the more realistic.

Liquidation value of land, road property, equipment and other physical property—in general.—The gross liquidation value of land and physical property estimated by the NH trustees is $70.8 million in excess of the estimate of Penn-Central, as detailed below:

Class of property and ICC account number	NH trustees	Penn-Central	Difference
	000	*000*	*000*
Land (2)	$107,412	$66,768	$40,644
Bridges, trestles and culverts (6)	(1,418)	(3,435)	2,017
Ties (8)	8,501	3,578	4,923
Rails (9)	30,756	22,657	8,099
Other track material (10)	8,610	5,486	3,124
Track laying and surfacing (12)	(10,967)	(8,649)	(2,318)
Other road property (11-45)	4,358	2,955	1,403
Total for road	147,252	89,360	57,892
Locomotives (52)	690	1,074	(384)
Freight-train cars (53)	8,090	3,455	4,636
Passenger-train cars (54)	9,998	3,086	6,911
Floating equipment (56)	3,170	1,280	1,890
Work equipment (57)	581	171	110
Miscellaneous equipment (58)	422	5	417
Total for equipment	22,851	9,071	13,580
Miscellaneous physical property except Grand Central properties (737)	3,537	4,192	(655)
Total all land and physical properties except Grand Central	173,440	102,623	70,817

Liquidation value of land (ICC account No. 2).—An overall valuation of the real estate was made by NH's general real estate agent who relied in some instances on appraisals made by independent appraisers. These appraisals principally covered the Oak Point and Harlem River freight yards in the Bronx section of New York City and the NH office building in New Haven, Conn. Land valuation for Penn-Central was made by Central's general real estate manager. The Penn-Central valuation is $40,644,134 less than the liquidation value shown in the trustees' study. Of this difference, $2,505,990 applies to the Harlem River Yard ($1,344,900) and to the Oak Point Yard ($1,171,090), and $38,138,144 applies to other land.

Substantial differences in the respective studies are as follows:

	Land valuation		
	Acres	NH trustees	Penn-Central
Boston Terminal-South Bay Jct.	145.11	$6,458,634	$4,880,243
Fort P. Channel-South Bay	46.62	1,641,450	688,000
Conn. State line-Springfield	97.18	1,928,089	1,475,360
Acorn Street-Smith Street	46.97	4,655,700	3,022,942
Providence-East Providence	23.02	1,043,451	62,490
West River-E. River (New Haven)	160.76	5,184,496	3,011,500
N. Y. State line-Stamford	256.50	6,610,830	5,874,916
Stamford-South Norwalk	166.33	2,411,892	1,306,785
Woodlawn-New Rochelle	64.83	3,185,785	2,357,405

The NH trustees assumed that sales would be in normal size parcels, with no unusual sales (such as for highway purposes); that outstanding options such as those held by the Massachusetts Bay Transportation Authority would be exercised; and that property values should be discounted 50 percent where railroad records indicated questionable title. Specific consideration was given to each part of the railroad's property, and values were reached on a zone-by-zone basis. Estimates of fair market value were based upon judgment, sales in the area, the record of existing railroad tax valuations, and adaptability of the property for other use. No weight was given to the possible impact of termination of NH operations on the real estate market generally.

Penn-Central obtained maps and information regarding NH real estate from NH's real estate department, and made their own field appraisals. They considered information regarding NH's title to property, the effect a defective title might have on salability, and current zoning regulations. In making the valuation Penn-Central used the same ground rules as NH, including the latter's zone-by-zone basis. They used per-square foot or per-acre unit value where appropriate. Also considered was the extent to which discontinuance of railroad operations might tend to restrict salability of lands and require subdivision into smaller parcels, but no consideration was given to the impact of discontinuance of rail service on the economy of the affected region or its real estate market.

From 1956 to 1965 NH handled 1,668 sales of property involving more than $31 million. In 1962 through 1965 alone, 702 sales were completed for a gross consideration of $12.5 million, and during the entire trusteeship through November 1966, a total of 853 sales were completed for a gross consideration of about $13.9 million. This large volume of past sales provides a firm base for NH's appraisal of the liquidation value of its land. The record supports the NH trustees' estimate of land valuation.

Chase argues that the real estate unsold at the end of a 6-year liquidation period was excessively discounted to the extent of $8 million because the initial appraised market value was placed too low to warrant such discounting. Chase's argument is not sustained by the evidence.

Since Gruss submitted evidence concerning the Harlem River and Oak Point yards, a more detailed discussion of the valuation of those properties follows.

HARLEM RIVER AND OAK POINT YARDS

The liquidation values placed on the subject properties, including buildings, were: (1) by the NH trustees, $18,090,990; (2) by Penn-Central, $15,585,000; and (3) by Gruss, $32 million. Penn-Central's valuation is deficient because of its forced sale concept, contrary to Penn-Central's overall approach to the valuation of NH's properties. Rather than a forced sale of the Harlem River and Oak Point yards at an inauspicious moment, Penn-Central's overall evidence supports the proposition that these properties could be held until an advantageous offer is received. Both the NH trustees and Gruss consider these two properties to be readily marketable.

The difference in valuation between the NH trustees and Gruss is that the former value the property from the standpoint of industrial use while the latter considers it from a best-possible-use viewpoint, i.e., for housing.

We may pretermit the controversy between Penn-Central and certain of the creditors as to whether it is permissible, as a matter of law, to value the property on the basis of best possible use. Gruss' valuation, based on housing purposes, is at best speculative because of the requirement for a zoning change, and, in any event, could not be accomplished for some time to come because of outstanding long-term leases held by some of the tenants occupying the premises.

Based on the foregoing, we find the valuation of the NH trustees to be the most accurate and accept their appraisal of $18,090,990.

VALUATION OF BRIDGES, TRESTLES AND CULVERTS (ACCOUNT NO. 6)

Both Penn-Central and the NH trustees place a negative valuation on bridges, trestles and culverts; that is, they estimate that the cost of removing the structures would exceed the selling price. As shown below, the estimated negative value in the Penn-Central study is $2,016,998 greater than in the trustees' study.

	NH trustees	Penn-Central
Value of steel recovered	$2,643,200	$1,345,200
Cost of removing	(4,061,300)	(4,780,298)
Difference		2,016,998

The difference is due principally to Penn-Central's use of a lower gross-ton value for recoverable steel and a higher removal cost per gross ton, as reflected below.

	NH trustees	Penn-Central
	Gross ton	
Structural steel recovered price	$20.00	$11.40
Cost to remove and sell truss and trestles	34.00	
Major structures, including piers		60.00
All others		34.00
Girders and beams	28.00	28.00
Timber bridges (trustees $43,047 Penn-Central $86,094)	3.00	6.00

The Penn-Central value for steel is reduced on the assumption that this material could not be disposed of in the New England market. No such reduction was made by the trustees. Creditors, agreeing with the trustees, believe that the material could be disposed of through major scrap dealers in Boston, New Haven and New York who purchase large quantities of scrap for export.

As in the case of steel recovered from the track, discussed later, it is fair to conclude that in a total liquidation of NH a substantial portion of the structural steel in the bridges—as much as 15 percent—would be sold outside the immediate New England market, with resulting transportation charges and a lower net price. The value of the steel is so treated in our present valuation of New Haven and in determining fair and equitable terms.

With respect to the bridge material, Penn-Central estimates that the cost of removal of major structures, including piers in navigable waters, would be $60 per gross ton, compared with the figure of $34 in the trustees' study. The $60 figure in the Penn-Central study includes removal of piers in navigable waters (in the case of major structures), whereas this cost is not referred to in the trustees' study. Some creditors contend that many of the piers involved in the bridges would not have to be removed, but it is fair to conclude that in a liquidation of NH some piers over navigable waters would have to be removed, resulting in added cost.

We have increased the $1,418,000 net cost in the NH study by $354,000 to take account of the aforementioned factors.

VALUATION OF TIES (ICC ACCOUNT NO. 8)

Crossties.—The Penn-Central valuation of crossties is $4.9 million less than that of the NH trustees. This difference arises from Penn-Central's assumptions that, in a total liquidation of NH, only a limited number of crossties could be disposed of in the New England market and that shipping ties for sale elsewhere would result in substantial transportation costs. Accordingly, as shown below, the Penn-Central study differs substantially from the NH trustees' study in respect to the number of ties which could be recovered and sold.

	NH trustees	Penn-Central	Difference
Reusable number 1 crossties	2,111,217	930,000	1,181,217
Reusable number 2 crossties	1,418,218	650,000	768,218

The creditors agree with the NH trustees that the net price of all usable ties would be attractive to other railroads and to New England firms which deal in relay track material.

Penn-Central contends that a successful marketing program for the ties would be impossible unless it would be in a position to purchase large quantities of the used NH tie material and that if Penn and Central merge, they will generate more than enough such material from their own dismantlings.

Bridge and switchties (other than crossties).—As shown below, the trustees and Penn-Central differ in respect to quantity and price of bridgeties that could be disposed of and the price of switchties.

	NH trustees	Penn-Central
Bridgeties—thousand board feet	6,973	1,629
Price	$92	$40
Total value	641,516	65,160
Switchties—price	72	60
Total value	618,696	515,580

Penn-Central believe the only bridgeties reusable would be those placed by NH during the last 10 years. The price of $40 per thousand board feet for these ties is 20 percent of $200 per thousand board, represented by Penn-Central to be the approximate price of new ties. Involved also in the Penn-Central price are the cost of removing, treating, and framing ties for reuse.

In Penn-Central's judgment, the following number of units could be marketed at the prices shown:

	Thousand board feet	Price per thousand[1]
Bridgeties–3-year period	300,000	$60
Switchties–3-year period	600,000	60

[1]Maximum retail price loaded on freight cars.

Penn-Central argues that to sell the entire quantity of ties involved in a NH liquidation would present a nearly impossible marketing problem. This argument is wanting in that it is largely predicated on the anticipation that the Penn-Central merger would throw substantial amounts of used ties on the market. However, the record shows that Penn-Central do not intend to abandon substantial segments of their road and, at any rate, no abandonment can be effected without our authorization. Moreover, its lines of track would be altered only to a minor extent by the closing of yards and reduction of double track to single track.

We conclude that the total quantities of ties (cross, bridge and switch) shown by the NH trustees and supported by creditor groups could be sold either in the New England market or elsewhere. The Penn-Central study indicates quantities that could be sold in the New England market. We believe that a large portion of the remainder—as much as one-half—could be disposed of in other nearby locations with little transportation costs. The balance would incur substantial costs for transportation to more distant markets. Consequently, we have reduced the NH trustees' estimate by $758,000.

VALUATION OF RAILS (ICC ACCOUNT NO. 9)

The Penn-Central valuation of rails is $8.1 million less than the NH trustees'. The principal difference is in the price per gross ton placed on rails by the respective parties, although some difference exists in the quantity of rails each party counted as recoverable. The differences are shown below.

	NH trustees		Penn-Central	
	Gross tons	Price	Gross tons	Price
Relay rail	211,842	$90	209,060	$65
Reroller rail	63,521	55	62,887	44
Scrap rail	163,938	50	161,785	39

Penn-Central employs the same $90 per gross ton for relay rail as is used by the trustees, but reduces the price 15 percent for market "flooding" and $11 per ton for transportation costs. The net prices for reroller rail and scrap rail were computed by deducting a transportation allowance.

Creditor groups support the trustees' prices, contending that the New England market (Boston, New York and New Haven) could absorb the material at prices comparable to those estimated by the trustees. They also assert that, upon liquidation of NH, substantial segments of the line would very likely prove salable to other carriers, particularly connecting carriers. The trustees contend that either of these factors would reduce or eliminate transportation costs and minimize the danger of flooding the market.

Penn-Central considers its price of $65 per gross ton for relay rail is a fair and reasonable estimate of what NH could obtain in a total liquidation. They also consider their $44 per gross ton estimate for reroller rail to be the maximum obtainable and the $39 per gross ton for scrap rail to be high.

As in the case of ties discussed previously, we conclude that, in a total liquidation of the NH, a substantial portion of the relay rail, roller rail, and scrap rail—as much as 15 percent—would be sold outside New England and other nearby markets, resulting in transportation costs and a lowered net price. The NH trustees' estimate is adjusted downward by $1,170,000 to reflect this conclusion.

VALUATION OF OTHER TRACK MATERIAL (ACCOUNT NO. 10)

The Penn-Central valuation of other track material (tie plates, angle bars, scrap, et cetera) is $3.1 million less than the NH trustees' valuation. As in the case of rail, the principal difference is in the price used by the respective parties. The trustees, supported by creditor groups, based their valuation on a price per *gross* ton, 2,240 pounds; Penn-Central's valuation was founded on a price per *net* ton, 2,000 pounds, as set forth below.

	NH trustees		Penn-Central	
	Gross tons	Price	Net tons	Price
Track material	63,906	$90	56,311	$65
Scrap	71,463	40	62,962	29

As to this account, Penn-Central takes substantially the same position as they did for rail, namely that a total liquidation of NH would flood nearby markets and, therefore, entail shipping costs. As in the case of ties and rails, we conclude that a substantial portion of this material would have to be sold outside the New England market, thus lowering the net proceeds. The NH trustees' valuation is reduced by $358,000 to reflect these factors.

TRACK LAYING AND SURFACING (ACCOUNT NO. 12)

For this account Penn-Central shows a negative amount of $8.6 million compared with a negative amount of $10.9 million shown by the NH trustees. Thus, Penn-Central would reduce the NH liquidation figures by $2.3 million. The negative amounts, in each case, are the estimated costs of removing rails and ties and such costs are applied by the respective parties to reduce the gross proceeds of a sale. Both parties employ the same cost per mile for rail and per unit for ties removed, but they differ substantially as to the number of miles and units.

Having accepted the NH trustees' estimate of track materials to be removed and sold, we should accept their estimate of the removal cost.

LOCOMOTIVES (I.C.C. ACCOUNT NO. 52)

The NH trustees' net valuation for locomotives, as shown below, is $383,300 less than the Penn-Central's.

Line No.		NH trustees	Penn-Central
1	131 locomotives	$1,004,700	$1,004,700
2	23 1,000-horsepowered diesels	154,000	69,000
	Total	1,158,700	1,073,700
3	10 electric locomotives	1,000,000	(Excludes $3,600,000 on
4	36 2,500-horsepowered diesels	5,400,000	which obligations cannot be
	Total	7,558,700	disaffirmed)
	Deduct equipment obligations[1]	6,868,304	
	Net value of locomotives	690,396	1,073,700
	Difference		383,304

[1]Comprised of $892,000 with respect to the 10 electric locomotives and $5,976,304 as to the 36 diesels.

Where obligations on particular equipment exceeded the estimated sales price, the equipment was excluded from the valuation

by both the trustees and Penn-Central on the assumption that the obligations would be disaffirmed. The amounts so excluded were $8,100,000 by the trustees and $3,645,000 by Penn-Central. An exception occurred in the case of the 36 2,500-horsepowered diesels (though the trustees value them at $576,304 less than the amount owed thereon), because the obligations could not be disaffirmed. Penn-Central excluded those 36 units from their valuation, considering the amount a liability rather than a valuation factor.

As to items 3 and 4 in the above table the trustees' valuation exceeds the Penn-Central valuation by $193,000, consisting of an $85,000 greater value on 23 1,000-horsepowered diesels and $108,000 greater value on 10 electric locomotives. Although in both cases the valuations are based on the general knowledge and judgment of the evaluators, we accept the figure of the NH trustees.

VALUE OF FREIGHT CARS (ACCOUNT NO. 53)

The NH trustees' net valuation of freight cars is $4.6 million in excess of Penn-Central's. The latter's valuation is lower because it utilized lower prices and was made as of December 31, 1966, 1 year later than the trustees', and does not reflect several hundred cars retired since the date used by the trustees. The details are shown below.

Type of car	NH trustees		Penn-Central	
	Units	Value	Units	Value
Boxcars—40 foot	2,929	$5,098,400	2,024	$2,024,000
Boxcars—insulated	103	412,000	98	196,000
Hoppers—open	538	1,614,000	538	807,000
Flatcars (year 1962)	50	500,000	50	125,000
Cabooses	190	465,000	183	274,500
Other freight cars	502	661,025	500	468,398
Total	4,312	8,750,425	3,393	3,894,898
Deduct equipment obligations	-----	660,000	------	440,000
Total	-----	8,090,425	------	3,454,898
Difference	-----	---------	------	4,635,527

Amounts excluded from the valuations for freight cars subject to equipment obligations estimated to be disaffirmed in an assumed liquidation were $348,000 for the trustees and $265,000 for Penn-Central.

Boxcars—40 foot.—The trustees valued 2,929 uninsulated 40-foot boxcars at an average price of $1,740 per unit; Penn-Central valued 2,024 units at a price of $1,000 per unit, resulting in a lower Penn-Central valuation.

The record shows that NH recently sold 100 cars for $2,350 each and that such cars were not suitable for general operation without heavy repairs. In these circumstances, Manufacturers argues that the recent sale price is the standard which should be used. The sale of 100 cars at a price of $2,350 each does not indicate that sale of a fleet of over 2,000 cars would produce that same price for each unit. In our judgment, the evidence supports the price per car of $1,740 used by the trustees.

Boxcars—insulated.—The NH trustees' unit valuation of these cars was $4,000 compared with Penn-Central's value of $2,000 a car. Creditor groups support the trustees' value. They argue that the lower Penn-Central value reflects an arbitrary reduction in valuation of 50 percent. Penn-Central argues that modern insulated cars are 50-foot, 70-ton cushion cars; that it is impractical to modernize and lengthen a 40-foot insulated car; that there would be small demand, if any, for such cars from any railroad and that the market for such cars is virtually nonexistent. Penn-Central believes the cars would be sold for scrap in the neighborhood of $500 per car, and that few sales, if any, could be made at prices in excess of $2,000 per car.

Manufacturers argues that these insulated boxcars are, on the average, 6 years newer than the NH uninsulated boxcars and that the Penn-Central valuation of the newer insulated cars is only $2,000 per car, twice the value it places on the uninsulated cars, but still less than the price at which the NH sold older 40-foot uninsulated cars (the $2,350 referred to above). Manufacturers asserts that these newer 13-year-old insulated cars should be valued on a basis of service life proportionately higher than the trustees' $1,740 unit-value for the older 19-year-old uninsulated 40-foot cars and that, on such basis, the trustees' value of $4,000 a car is conservative.

We consider the trustees' unit valuation for these 13-year-old cars to be fair and reasonable.

Open hopper cars.—The trustees valued the 538 open hopper cars at an average price per unit of $300; Penn-Central decreased the price by 50 percent, both parties relying on judgment. These units were approximately 12 years old at the close of 1965. We accept the trustees' valuation as reasonable.

Passenger cars (account No. 54).—The NH trustees' valuation of passenger cars is $6,9 million more than Penn-Central's. The latter was made 1 year later, with eight fewer units. As shown below, the principal difference is in the pricing of equipment.

Type of cars	NH trustees		Penn-Central	
	Units	Value	Units	Value
Old steel coaches	199	$144,000	199	$144,000
Stainless steel	110	2,800,000	110	666,000
Parlor lounge	40	932,500	39	195,000
Sleeping cars	26	520,000	26	130,000
Head-end cars	150	150,000	144	96,400
Diner and grill	27	941,000	26	130,000
Old electric motor	2	2,400	2	2,400
Old trailer coaches	36	28,800	36	21,600
New electric motor (a)	100	6,000,000	100	3,000,000
Budd cars	39	885,000	39	390,000
Roger William	6	150,000	6	15,000
Total	735	12,553,700	727	4,790,400
(a) Less equipment obligation	------	2,556,000	------	1,704,000
Total	------	9,997,700	------	3,086,400
Difference	------	----------	------	6,911,300

The above valuations exclude equipment where obligations could be disaffirmed. The amounts so excluded are $300,000 for the trustees and $75,000 for Penn-Central.

The four principal categories of passenger equipment in which important differences exist are the stainless steel, parlor lounge, diner and grill, and new electric motor cars. The unit values used for the four categories of equipment are:

Class of cars	NH trustees	Penn-Central
Stainless steel cars	$25,454	$6,054
Parlor lounge	23,310	5,000
Diner and grill	34,888	5,000
New electric motor	60,000	30,000

Penn-Central estimates that stainless steel cars have an average age of 18 years; that demand for this type of car is limited; and that the placing of 110 cars on the market would drive the prices down markedly. They argue that the market is even more limited for parlor lounge cars (18 years old in 1966); and for diner and grill cars.

With respect to the 100 electric motor cars (average age 12 years in 1966), Penn-Central assert that, only three railroads in the country use this type of car—Central, Penn, and the Long Island Railroad Company; that Penn and Central would not be

interested in purchasing 100 cars and that under no circumstances would they purchase them at a price approaching the $60,000 per unit valuation used by the trustees.

Penn-Central believes there is no significant market within the United States for sale of used passenger equipment; that the market in Canada is also limited; that the Mexican market has approached the saturation point; and that NH would not be able to realize a sum even as large as the $4.8 million estimated by Penn-Central.

The creditors agree generally with the trustees' valuation and their evidence establishes that Penn-Central's valuation of these cars is much too low. The purchases of Penn and Central in recent years of passenger cars, shown on the record, are not relevant here because there is no showing of comparability between the cars involved in those transactions and NH cars. On the other hand, much of the evidence of record indicates that the trustees' estimate of value may be too high when considered in the light of Penn-Central's opinion of the cars' salability and their need for rehabilitation. Accordingly, we conclude that, although they are basically reasonable, the trustees' estimates should be reduced by at least $3.5 million, or about 50 percent of the difference in the valuation discussed.

In general, the creditor groups accept the NH trustees' study but would build on to it. As previously noted, the gross value of the NH assets under the NH trustees' study is $230.3 million. The Committee contends the gross value is $424.6 million; Chase asserts it is $333.8 million; and Manufacturers maintains that it is more than $330 million. Those differences warranting comment but not previously discussed are considered below:

Investments.–The Committee would increase the valuation of investments by $11.3 million. The items in controversy are as follows:

Company	NH trustees	Committee	Increase
	000	*000*	*000*
Fruit Growers Express	$321	$1,424	$1,103
New York Connecting Railroad	----------	1,117	1,117
Pullman Company	200	495	295
Railway Express Agency	----------	1,827	1,827
Affiliated lines:			
South Manchester Railroad	65	90	25
Boston & Providence	4,682	11,178	6,496
Holyoke & Westfield	21	24	3
Norwich & Worcester	958	992	34
Providence & Worcester	1,085	1,487	402
Total	7,332	18,634	11,302

Fruit Growers Express.—The trustees' estimate of liquidation value is $95.54 per share, corresponding with the NH book value. The trustees are doubtful that other coowners would pay more. The Committee value of $423.41 per share is based on stockholders' equity.

New York Connecting R.—The trustees believe the stock has no liquidation value because of the approximately $18 million debt compared with remaining relatively small salvageable value of the property. The Committee points out that Penn-Central, in their joint petition for approval of the plan for inclusion of NH, values the equity of the NH interest at $1,117,415.

Railway Express Agency.—The trustees consider that the stock has little if any liquidation value because of litigation and recent legislation increasing the allowable size and weight of parcel post packages. The Committee value is $20 per share on 91,344 shares owned by NH on the basis of an offer of that amount, since withdrawn, by Greyhound Lines.

B&P.—The trustees' valuation of the investment in stock and debentures is $4.7 million, the book value. The Committee valuation is $11.2 million, the trustees' estimated liquidation value (including land) before deducting estimated liquidation expenses of $3.1 million. The estimated net liquidation value of B&P land is $8.1 million.

P&W.—The trustees' valuation of $1.1 million is based on net liquidation value of physical property less principal and accrued interest on books, equivalent to $113.57 per share on 9,551 shares. The Committee valuation is $402,000 more, after elimination of estimated liquidation expenses.

We are persuaded that the estimates of the NH trustees are reasonable. The creditor groups presented no witness of their own in this area, and the expertise of the sponsoring witness for the NH trustees and the care with which he made his analyses are unquestioned.

Chase protests that no value has been ascribed to the CCBI's to be issued in connection with the B&P reorganization. But under the transaction proposed herein, Penn-Central would acquire the B&P properties subject to the equitable charge of the CCBI's to be issued to the public stockholders of the B&P. Thus, the CCBI's would be more of a liability than an asset. Even if construed to

be an asset, there is no firm basis for assigning any value to them.[15]

Sale to other railroads.–Chase maintains that the NH trustees fail to recognize that other railroads will be in the market for substantial portions of NH assets. Chase claims that this would not only substantially increase the proceeds of liquidation but make unnecessary any demolition work.

Despite the surmising about the probable interest of other railroads, the simple fact is that no other railroad has displayed an interest in purchasing any portion of NH. We are not persuaded by Chase's argument.

Grand Central Terminal properties.–NH's recorded investment in the Grand Central Terminal properties is $19,953,930, of which $10,453,930 is represented as unrefunded building advances and $9,500,000 as advances for capital improvements such as furniture and fixtures.[16] There is also recorded on the NH's books $1,522,840 represented as uncollected excess of income derived from the Grand Central Terminal properties.

The NH trustees do not believe that NH has ownership in the fee or that it possesses rights independent of continued operation into Grand Central Terminal. Their counsel has advised that NH's rights are dependent on use of Grand Central Terminal and that in the absence of such use NH is entitled only to reimbursement of construction advances. To preserve NH's rights, the NH trustees brought suit to collect excess of income in 1964 and 1965 which Central denied them. Nevertheless, the trustees contend that to the extent resolution of the controversy over NH's

[15]The district court, in approving the B&P plan of reorganization, said (260 F. Supp. at page 419):

The first two of the Development Group's objections are directed against the provisions incorporated in the plan with respect to the CCBI's. These provisions were included because of the potential value of certain portions of the debtor's real estate, based on the price which would be received for this land if it should be sold or taken for highway or rapid transit purposes. There is, of course, no certainty that any of this land can be disposed of and hence no firm basis for including this contingent value as an element in the compensation to be paid by the New Haven for the debtor's estate. Therefore the plan includes the CCBI provisions as a device for assuring the public stockholders of the debtor of their fair share of any "windfall profit" should any of these potential values materialize within the reasonably immediate future.

[16]Under section 1.10 of the purchase agreement, "The term 'Grand Central Terminal Property' shall mean all property, real, personal and mixed (together with all rights pertaining thereto), including land and interests in land, and all improvements thereon, which property is in the area between 42nd Street on the south, 60th Street on the north, Madison Avenue on the west, and Lexington Avenue on the east, in New York, N. Y., and is the subject of agreements, dated 1848, 1872, 1907, and 1913, or of other particular agreements, between the New Haven and Central, or respective predecessors."

rights may be considered a thing of value the agreement with Penn-Central covers such value. If their position should be wrong, the NH trustees indicate the consideration provided in the agreement is inadequate.

Penn-Central maintain that NH's only interest in the Grand Central Terminal real estate is its rights to repayment for construction advances for the Hotel Waldorf-Astoria which they claim amount only to $1.1 million. Otherwise, they assert, such rights as NH may have in the properties are dependent upon continued passenger service into the terminal. Moreover, they contend that even if NH should continue to use the terminal, the maximum right it would have to income from the properties is free use of the terminal.

The creditors argue that, as regards the Grand Central Terminal real estate ventures, NH is a partner or owner of the fee in common with Central. The claims of the creditors range from $20 million to $115 million, the latter being 50 percent of the value of the Grand Central nonoperating properties as developed in an independent appraisal made on behalf of the NH trustees.

It is not within our jurisdiction to fix NH's legal rights, if any, in the Grand Central Terminal properties. *Boston & P. Reorganization, supra,* 327 I.C.C. at page 15. Our function is to value the claim. *Freeman* v. *Mulcahy,* 250 F. 2d 463, 475 (1st Cir. 1957), *cert. denied sub nom., Boston & Providence Railroad Corp.* v. *New York, New Haven & Hartford Railroad Co.,* 356 U. S. 939 (1958); *Boston & Providence Railroad Corp., supra,* 260 F. Supp. at page 421.

The basis for the controversy is a 1907 agreement pursuant to which Central "doth demise, let and lease" to NH the use of the "railroad terminal" in common with Central. "Railroad terminal" is defined in the agreement to "mean and include the land, and interests in land, and all improvements thereon (not including the distributing system hereinafter mentioned), and all rights in any ways on which said land may abut."

The parties decided in 1909 to utilize the surface of the property and, pursuant to agreements NH and Central jointly financed the construction of certain buildings. In 1913 the parties added language to the 1907 agreement as if such language had been part of the original agreement "to express more fully the intent of the parties with respect to the construction, maintenance and use of such buildings and with respect to the rentals accruing from the lease of such buildings or portions thereof."

Pursuant to the 1907 and 1913 agreements several hundred agreements were reached relating to the leasing, financing, and sharing of rentals from the buildings constructed in the terminal area. Rentals and other compensation from these properties are credited to the fixed charges and cost of maintenance and operation of the railroad terminal.

The contract for sale of NH assets to Penn-Central provides that the property shall include, without limitation, all the New Haven's right, title and interest in and to (a) Grand Central Terminal property on the closing date, and (b) the amount of any judgment against or recovery from Central resulting from any action commenced by the trustees subsequent to the date of this agreement based on a claim with respect to the excess of income derived after 1963 from Grand Central Terminal property over the aggregate expenses after 1963 for the joint operation by Central and the New Haven of Grand Central Terminal.

The express provisions in the agreement among the NH trustees and Penn and Central as well as the emphasis placed in a Central proxy statement to shareholders indicate that Penn and Central believe they are obtaining a thing of value in the release of the NH rights in Grand Central Terminal properties.

There has been much debate over whether the NH interest in the Grand Central Terminal properties, other than with respect to unpaid building advances, would expire if the NH should cease service.[17] If that should be the case, from the standpoint of a liquidation value, the worth of the NH's interest in the properties would be diminished.

As indicated, the NH trustees, relying on opinion of counsel, are persuaded that NH interest would not survive an end to service. Despite that opinion, a valid argument can be made that NH's interest in the Grand Central Terminal properties does not terminate with a cessation of service. The opinion rests on an interpretation of the implicit meaning of the contracts. However, there is no express requirement in the 1907 and 1913 agreements that the NH exercise its right to use the Grand Central Terminal.

Other features of the agreements lend support to the proposition that NH's interest in the Grand Central Terminal properties is not bottomed completely on use of the terminal. The payments

[17] In the *NH Train Discontinuance* case, *supra*, 327 I.C.C. at page 199, we said, "If its (NH's) passenger service were discontinued, all of its income from the Grand Central Terminal properties, with minor exception (Waldorf-Astoria), would cease." But no party contends that we are bound by that statement and the issue cannot be raised on the ground of collateral estoppal. The matter has been fully developed in the instant proceeding, and we shall make our findings on the basis of the record herein.

NH is obligated to make are computed from NH's and Central's relative car and locomotive use of the railroad terminal. While this is basis for the contention that NH's interest is dependent on use, the 1907 agreement imposes upon NH a minimum charge of $160,179.92 each year regardless of the extent of its use. On the basis of the foregoing it can be reasonably argued that the NH's rights are not founded solely on use. Moreover, under the view that those rights cease when NH ceases operating passenger service into the terminal, Central could demand the minimum charge as long as it deemed such action advantageous and then dispossess NH whenever that might produce a more favorable result for Central. This gives all the options to Central. It is arguable whether this can be accepted as the intent of the parties to the contract in light of the substantial contributions the NH has made to the development of the terminal properties. *New York Central R. Co.* v. *New York, N. H. & H. R. Co.*, 13 A.D. 2d 309, 216 N.Y.S. 2d 928 (1st Dept. 1961), affirmed, 11 N.Y. 2d 1077, 184 N. E. 2d 194 (1962). (The *Biltmore* case).

In addition to the 1907 and 1913 agreements, the subsequent agreements between the parties are equally important to an assessment of the rights of the NH and Central in the terminal properties. They not only grant rights but place heavy responsibilities on the NH and Central. For example, the contract leasing the Hotel Barclay to New York State Realty and Terminal Company (Realty Company), a Central subsidiary, provides that Realty Company shall provide at the cost and expense of Central and of NH such additions and improvements to the Hotel Barclay and such additions, improvement and renewals of the furniture, furnishings and equipment thereof as may be approved by Central and NH. Furthermore, NH and Central have convenanted that, in case the Hotel Barclay operation in any year results in a net deficiency, they would pay the Realty Company upon demand, any such deficiency—each contributing one-half of the amount of any such deficiency.

We cannot assume that NH's obligations under these contracts end if it should cease to operate into Grand Central Terminal. Certainly, in the *Biltmore* case, *supra*, which sustained the right of NH to join on an equal basis with Central in a lease of the Hotel Biltmore properties, the court expressed doubt as to the ease with which NH could relinquish its obligations under these contracts. (216 N.Y.S. 2d at page 937). It is reasonable to conclude that NH would not have embarked on such real estate ventures

unless it anticipated that it would enjoy the benefits thereof regardless of whether its rail operations continued. See *Biltmore* case, 24 Misc. 2d 414, 208, N.Y.S. 2d 605, 615 (Sup. Ct. N.Y. Cty. 1960); 216 N.Y.S. 2d at pages 934; 936–937.

While we are not empowered to establish the legal rights of NH in the terminal properties, we are convinced that NH has substantial support for a claim that its rights and interests survive even if its passenger service into the terminal stop.

Regarding the value of this claim of right, Penn-Central and the NH trustees make much of the undisputed fact that Central is the fee simple owner of the properties. However, this does not have overriding significance. See *Biltmore* case (216 N.Y.S. 2d at page 936). Penn-Central urge that even if NH's operations continue, the ceiling on NH's right to income is free use of the terminal. They claim that the agreement is a joint facility agreement in which the grantee does not acquire rights to profits of ownership. In addition, Penn-Central contend that under the 1907 and 1913 agreements and the agreements involving specific terminal properties, the rentals or other compensation are to be credited to the expenses of the terminal operations as a deduction from costs.

There are substantial arguments to the contrary. If the agreement is a joint facility agreement, it is most unusual and to label it a "joint facility agreement" is not helpful in ascertaining the rights of the parties. We have already disposed of Penn-Central's contention that ownership of the property is of importance. With respect to the "credited" language above, it is unreasonable and unfair to conclude that the NH would enter into agreements for development of terminal properties with obligations equal to those of Central but with rights to benefits inferior to those of Central. Cf. *Biltmore* case, 216 N.Y.S. 2d at page 934.

Penn-Central's suggestion that the value of the terminal to NH is only $1.1 million in unpaid construction advances is rejected, since Central indicates that NH's claims have a $5 million "nuisance value."

We do not believe justified, however, the position of creditor groups that the value of NH's interest is $115 million, one-half the appraised value of the Grand Central Terminal nonoperating properties.[18] The rights asserted on behalf of NH in the terminal properties have not been established by any court and if the matter

[18] Unpaid building advances and other capital investments in Grand Central properties are carried on the NH books of account at $20 million.

were litigated, the outcome could not be predicted. In fact, the opinion of the trustees' counsel appears to be that NH would not prevail in such litigation. We only decide here that the claims of NH are not frivolous but claims of substance, and in the absence of litigating them, they must be deemed to be valuable.[19]

The fact that NH's interest in the Grand Central Terminal properties is not freely alienable adversely affects the value of its interest. However, it appears that transfer of Central's interest in the properties would require NH's participation. Thus, Central's acquisition of NH's rights adds to the value of Central's interest.

Manufacturers suggests a method for valuing the NH interest in the Grand Central properties based on the estimated excess income above Terminal costs. For this purpose, Manufacturers employs an NH share of such income in the amount of $1,998,000 on a 40-percent car-use basis. Assuming a 50-percent interest for NH and capitalizing the income at a rate of 5 percent, Manufacturers indicates a value of $50 million.

Until recently, no excess net income was realized from the Grand Central Terminal properties. However, in 1964 and 1965 such income was earned. NH claims that its portion of the income, on a car-use basis of approximately 40 percent, is $1,842,401 for 1964 and $1,473,627 for 1965, or an average for the 2 years of $1,658,014. Capitalized at 8 percent a year, which we believe to be a realistic rate, this annual average income would have a value of approximately $20 million. In our judgment, after taking all relevant factors discussed above into consideration, the value of NH's interest in Grand Central lies between the foregoing capitalized income average and the $5 million Central assigns to the NH interest as nuisance value, or approximately $13 million. We so find.

Other elements of value.—The creditors contend that NH has value as a going concern over and above the liquidation value of its physical properties. We are not convinced that NH as a going concern has a greater value than it has in liquidation.

The creditors vastly overstate the value of the various elements embraced in their going concern valuation study. They would assign a total of $55,075,000 to such intangibles as organizational

[19]Ehrenclou has proposed that the Grand Central Terminal properties dispute be resolved in the courts before inclusion of NH in Penn-Central is permitted. We believe a decision on the overall valuation without having this matter litigated is warranted at this time.

costs, including engineering expenses and interest during construction, utilizing historical costs without regard to the probability that NH in its present form would never be built today. These intangibles should be assigned a value no greater than 10 percent of the creditors' estimate.

The creditors disagree with the deduction by Penn-Central and the NH trustees of the amount of equipment obligation Penn-Central will assume on NH rolling stock. They contend that since Penn-Central will acquire all of the rolling stock, its full value should be added to the liquidation value previously discussed. We believe, however, that the value of the rolling stock, if NH were sold as a going concern, would be offset or diminished by equipment obligations thereon. Thus, very little, if any, weight can be given to this item as an element of value.

It would appear, and the NH trustees and the creditor groups contend, that the values of the Harlem River and Oak Point yards are greater for an operating railroad than for a railroad in process of liquidation. The additional $8.0 million which the creditors would assign to the value of these yards for an operating railroad would appear unduly high in view of the past history of NH's operation. In our view, the $4.6 million enhancement estimated by the trustees is more realistic than the estimate of the creditors.

Federal income tax benefits Penn-Central may obtain through purchase of NH assets allegedly consist of NH's net operating loss carryforwards and the acquisition of the NH property basis. Chase claims that the NH tax attributes have a value of at least $10 million. Manufacturers submits that the value is approximately $20 million, consisting of $4 million for net loss carryforwards and $16 million for a tax basis advantage. Gruss urges that the tax benefits are worth at least half the total consideration to be paid by Penn-Central, which it estimates at $87 million, thus placing the value of the tax benefits at $43.5 million.

The Committee takes the position that, since the tax benefits cannot be precisely determined, provision should be made to revise the price paid by Penn-Central in an amount equal to the tax-savings to which Penn-Central may lawfully be entitled in the future. All parties agree that, unless some tax legislation is passed, Penn-Central will not secure NH's net operating loss carryovers.[20]

In all the circumstances we are persuaded that no specific value should be accorded the tax attributes in appraising the worth of

[20] As of December 31, 1965, they amounted to $82.7 million.

NH properties. Although we believe the NH tax features could be of value to Penn-Central, the actual gains are speculative as to time and amount. The advantage Penn-Central could realize from NH's net operating loss carryforwards is dependent upon the passage of legislation by the Congress, and, at this time, the likelihood of such action is yet in doubt. In the *N&W Inclusion* case, *supra*, we provided that, if such legislation should be passed, EL and B&M shareholders, the two carriers having net operating loss carryforwards, would thereupon become entitled to dividend paying N&W stock rather than the dividend-less stock of an N&W subsidiary. The proposal here before us contemplates the delivery of Penn-Central stock without a dividend limitation. This means not only the prospect of an immediate return but also opportunities for the future which NH now lacks. Therefore, in those respects, NH creditors are in a more favorable position than the stockholders of EL and B&M, since the immediate receipt by the NH Estate of Penn-Central stock is not contingent upon the passage of legislation. We believe that any dollar value attributable to a tax relief statute is necessarily highly speculative.

Penn-Central could possibly benefit from acquisition of the NH property basis, but any specific value assignable could only be speculative on the evidence of record. On the other hand, the recipients of Penn-Central stock will share in benefits which are entirely out of reach under NH's present deficit operations.

No party contends that NH's present scope of operations could be made remunerative. Even the creditor groups concede that NH's passenger service would have to be sustained through outside assistance or be discontinued if the freight service is to produce net earnings. In view of the essentiality of NH service and the possibility that unique measures may be required to preserve it, both the nature and scope of the passenger operations and the results of the freight service can be affected by events which we cannot foretell. In our judgment these circumstances call for considerable restraint in estimating the going concern value of the NH.

As presented by the creditors, we believe the "going concern value" is constructed upon an improper premise. As indicated, creditors would add the value of certain intangibles to the liquidation value of NH's assets. This method contains an inherent contradiction, and is unsound. It is not realistic to assume that a potential buyer would pay the liquidated value of the NH assets and then pay additional amounts representing elements of going

concern value in the face of NH's past deficit operations and its bleak prospects for the future. Rather than the approach used by the creditors, logic dictates that elements of going concern value be appraised in terms of NH as an operating railroad.

If there is one thing on this record that is clear and undeniable, it is that NH has neither earning power nor the prospect of earning power. Further, the facts preclude our finding that Penn-Central can, by some dramatic maneuver or otherwise, suddenly convert NH into a profit-maker. Standing as obstacles are such things as the economics of the particular environment, the unremunerative features of certain common carrier obligations, the carrier's compounded debt, the entrenchment of intermodal competition, and other factors—from which we cannot, in these transactions, fully insulate Penn-Central.

There was an attempt to show that as a freight-only operation NH could be made profitable, and it was established that Penn-Central today maintain a valuable freight traffic interchange with NH. On the other hand, the evidence shows that the continuation of passenger service could only be accomplished at a substantial deficit. We have found that, with the NH, the public's need for rail passenger service is on a par with the need for freight service, and have, therefore, made inclusion of both operations a condition to approval of the Penn-Central merger. Consequently, whatever validity there is to the freight-only concept, it is overwhelmed by the requirement that passenger service be preserved. Upon weighing the several relevant considerations, but with no pretense at mathematical precision, we are of the opinion and find that the total value of the NH sold as a going concern is less than its liquidation value.

It could well be that if a liquidation were attempted, governments or their agencies would take steps to preserve essential NH operations—either through contracts with private transportation agencies, takeover by governmental units, or some other means. Whatever the means, it is clear that the continued operations would be at a substantial deficit. The fair upset price, which would be the best price that NH owners could expect in those circumstances, would be lower in a condemnation proceeding than the liquidation value we are here assigning to the NH assets.

Calling upon Penn-Central to pay more than the NH is worth as a going concern is not unreasonable within the meaning of section 5(2). For the scope of our inquiry as to fair and equitable terms may reasonably go beyond the mere valuation of the carrier

to be acquired. The Penn-Central merger (which will bring substantial dollar savings to the merger applicants) was approved with the thought that some of the merger savings would be available specifically to ward off a liquidation and shutdown of the NH so that adequate transportation service would remain available to the public which now relies on the NH.

After considering the various positions of the parties in this case and their expert testimony, we are aware that valuations are not mere mathematical derivations but rest largely on judgment. The range of supportable values with respect to most of the items considered herein is wide. Based on our own judgement after analyzing and interpreting the entire record, we find that the liquidation value of the NH assets to be conveyed to Penn-Central is about $125 million as of December 31, 1966.

VALUE TO NH OF CONSIDERATION TO BE RECEIVED

On brief, NH takes the position that the value to it of the consideration to be received from Penn-Central is between $140.7 million and $148.3 million.

The Committee and Manufacturers value the consideration at only $98.2 million and $94.7 million, respectively. The following is a comparison of the three valuations:

Item	Committee	Manufacturers	HN Trustees
		Millions	
Penn-Central stock (950,000 shares)	$57.0	$51.7	$83.1
Penn-Central bonds (principal)	20.0	19.8	23.0
Cash	8.0	8.0	8.0
B&P bonds	3.0		
Equipment obligations	2.2	5.7	2.5
Labor protection	0.8		6.5 to 14.1
Pensions	0.5		5.1
Purchase price adjustment, section 9 of agreement	6.7	9.5	9.5
Total	98.2	94.7	140.7 to 148.3

The matters in dispute are discussed below.

Stock.—The trustees value Penn-Central stock at $87.50 a share, estimated as the market price at the date of closing under the purchase agreement. They believe that market value at the

time of inclusion will be in the range of $75 to $100 per share and use the midpoint price of $87.50 a share.[21]

The Committee values the Penn-Central stock at $60 per share. They assert that when the consideration between the parties was negotiated the market price of Penn stock was $41 per share and such price was used in deciding upon the terms of the agreement; that the Penn stock is now in the range of $60 per share; and that Penn stock has never sold as high as $75 during the past 10 years.

Manufacturers' value for the stock is based on a price of $54.40 per share, the average price at which Penn stock traded on the last trading day of each month for the 12 months ended May 31, 1967. Evidence presented by Penn-Central shows the shareholders' equity (or book value) of the Penn-Central stock after the merger to be $106 per share.[22] On the basis of issuance of 22,860,379 shares of Penn stock in connection with the Penn-Central merger, plus 950,000 shares to be issued for NH assets, pursuant to the purchase agreement, the NH stockholders' equity would be 4 percent of the total.

Penn-Central states that, on a *consolidated* basis the combined net income of Penn and Central for the year 1965 would have been $124,316,000.[23] On the basis of 22,860,379 shares of stock, after the Penn-Central merger, the net income per share would be, therefore, $5.44 per share. Capitalized at 8 percent, the value per share is approximately $68. After adding $81 million of anticipated annual merger savings (to the consolidated income) and deducting $8,476,000 estimated annual deficits of NH operations when it is included in the Penn-Central system, the combined income is $196,840,000. Assuming 23,810,379 shares of stock outstanding after NH's inclusion in Penn-Central, the income per share on a system consolidated basis would be approximately $8. Capitalized at 8 percent, approximately $100.

At the time in 1964 when the NH trustees and Penn and Central reached preliminary agreement on the terms of inclusion, Penn stock was selling at approximately $40 per share. Clearly the trend in the market price of Penn stock is up. On the basis of the evidence, it is fair to conclude that, for the purpose of deter-

[21] After reviewing the earnings of rail stocks in recent years and the railroad industry's future potentials, including recent earnings and market trends of Penn and Central common stocks, the NH Trustees conclude that an indicated price-earnings ratio or multiplier of between 12 and 14 for Penn-Central in 1972 would reflect an estimated fair market value at that time for the stock in a range of $144 to $196 a share.

[22] Appendix E.

[23] Appendices F and G.

mining the fair and equitable terms for inclusion of NH, the $87.50 per share value placed on Penn stock by the NH trustees is reasonable.

Bonds.—Under the purchase agreement the $23-million principal amount of bonds are to bear interest, not to exceed 5 percent, which would entitle them to a market value equal to their principal amount at date of issue. The NH trustees value the bonds at their principal amount. The Committee and Manufacturers contend that 5 percent railroad bonds do not currently trade at par.

The NH trustees assert that as of December 12, 1966, the price of the bonds would have been about $19.8 million and that a price equal to the principal amount would appear to be reasonable for the price potential of the Penn-Central bonds in 1972. On this basis, they would set the value at between $21 million and $22 million. Under the agreement, the basis for valuing the bonds is their date of issue. We believe this should occur well before 1972. In light of this consideration and other evidence of record, we are persuaded that the bonds should be valued at $20 million.

Equipment obligations.— The NH trustees believe that if Penn-Central does not assume NH's equipment obligations, the NH estate could reject all such instruments and become liable for the damage thus caused and that the parties whose contracts are rejected would be entitled to priority payment. They estimate that the value to the NH estate of not going through this process is equal to 10 percent of the principal amount of the obligations involved, which may aggregate $25 million at closing. Accordingly, they assign a value of $2.5 million to this portion of the consideration.

Manufacturers contends that the value of being relieved of equipment obligations is $1.4 million. They maintain that the NH trustees propose to pay off $10 million of such obligations, and the application of 10 percent to the remaining $14.3 million of obligations produces an estimate of $1.4 million.

The Committee argues that, if NH were to disaffirm these obligations, the equipment would be repossessed and the obligees would be general creditors for any balance due. It states that, in these circumstances, although the precise benefit, if any, to the NH estate of assumption of the obligations is difficult to compute, the estimate of the NH trustees is indefensible.

The position taken by the Committee is the most persuasive. Despite the opinion of the trustees that parties whose contracts are rejected would be entitled to priority payment, no such

treatment is proposed in their plan for reorganization. Under amendment No. 2 to the plan, any equipment obligations not assumed would be rejected. Ensuing claims would be treated as general unsecured claims on which no payment would be made. In these circumstances, we cannot ascribe any value to NH from Penn-Central's assumption of equipment obligations.

Labor protection and pension costs.–Penn and Central estimate the cost of labor protection at $19.2 million including pension costs. The NH trustees contend that $6.5 million[24] to $14.1 million for labor costs and $5.1 million for pension costs, should be considered as value to the NH estate.

Manufacturers and the Committee would reduce the value assigned to labor protection costs to $800,000 on the basis of revised labor protection costs of $8 million, or a total, including pension costs, of $1.3 million. Chase maintains that NH is under no legal obligation to pay any of these amounts. Therefore, no value should be ascribed to these items. It claims, moreover, that pension costs of $5.1 million are too high because a 3-1/2 percent interest rate used by the actuary is too low. Chase asserts that at a 5-percent rate the pension costs would be $4.1 million and at a 6-percent rate it would be $3.7 million.

Because of the liberal protection afforded NH employees, as later discussed, we find Penn-Central's estimate of $19.2 million for labor protection and pension costs to be more realistic and thus more reasonable than other estimates presented. It is noted that this figure conforms with the highest estimate of the trustees. There is no evidence to support Chase's contentions. However, there is no justification for attributing this estimated cost as value to NH.

Purchase price adjustments.–The purchase agreement provides for certain adjustments in the purchase price at closing. The record indicates that if closing had occurred on October 31, 1966, the purchase price would have been increased by $6.7 million. The trustees estimate that this represents an average annual adjustment favoring the NH estate since December 31, 1963, of approximately $2.3 million.[25] On this basis, they estimate that if closing were to occur on December 31, 1967, the purchase price would be increased by $9.5 million. The Committee challenges this

[24] This figure has been revised to $8.0 million.

[25] Central indicates that the very nature of this agreement allowing the New Haven to increase its price for all additions since 1963 shows clearly that the parties were intending to purchase the property as of December 31, 1963.

estimate. However, we find nothing in the record to rebut the trustees' estimate and it is, therefore, accepted.

Value to NH of consideration.—Based on the foregoing, we find that the value of the NH of the consideration to be received from Penn-Central is approximately $125 million. This conforms with the liquidation value previously found.

COST OF NH ASSETS TO PENN-CENTRAL

The differences concerning the cost to Penn-Central of acquiring the NH assets are exemplified by the following comparison of the valuations assigned by Penn-Central, the Committee, and Chase:

Item	Cost of NH to Penn-Central		
	Penn-Central	Committee	Chase
	(Millions)		
Stock, 950,000 shares (59 3/8 per share as of January 14, 1967	$56.4	$56.4	$56.4
Penn-Central bonds (principal)	23.0	23.0	23.0
Cash	8.0	8.0	8.0
B&P bonds	3.1	3.1	3.1
Equipment obligations	22.6	22.6	
Purchase price adjustment, section 9	6.7	6.7	
Refunds, side track	0.6	0.6	
Freight losses for 3 years	5.2		5.2
Pensions	5.0		
Employee protection	14.0		
Leased lines rental capitalized	5.3		
Depreciation for 1964-66	26.4		
Deferred maintenance	32.0		
Assets purchased, section 7	11.6		
Totals	219.9	120.4	95.7

Stock.—We have determined that the Penn-Central stock has a value to the NH estate of $83.1 million. The cost of this stock to Penn-Central for the purpose of acquiring NH's assets is the same amount, since value to the NH estate and cost to Penn-Central are measured by the same criterion, namely, market value at the time of issuance.

Bonds.—We have decided that the value of the Penn-Central bonds to the NH estate is $20 million. That decision was based essentially on market response. But no party contends that the cost to Penn-Central will be less than the $23-million principal, although the Committee points out that this does not mean a present cost. It was appropriate to discount the value of the NH

assets to present levels, because the inclusion contemplates a present conveyance to Penn-Central, whereas the gross valuations contemplated an assumed liquidation over an extended period. The discount brought the two concepts to a common ground. That procedure is neither necessary nor valid here, since Penn-Central will actually become obligated to pay the principal amount of the bonds. Therefore, we conclude that, for the purpose at hand, valuing the bonds at their face amount is reasonable. The same is true of the mortgage Penn-Central will assume with respect to the $3.2-million principal amount of bonds to be issued by B&P.

Equipment obligations.–Penn-Central estimated that it would assume equipment obligations in the amount of $22.6 million. The Committee does not protest recognition of this amount, but asserts that the obligations, falling due at various times until 1980, do not constitute a present cost. Chase, however, contends that the entire amount must be eliminated both to make the cost tabulation comparable with the NH trustees' liquidation value study and because Penn-Central is in a position to avoid any liability on the equipment. We will consider the full amount of the equipment obligations. Like the bonds, Penn-Central becomes liable for the full amount of the obligations assumed, and that amount is in fact the inescapable measure of its cost. The contentions of Chase are rejected as lacking substance, since the obligations assumed arise from the retention of equipment required to continue NH operations. Adjustments which would ignore these facts and the actuality of the cost would be fictional.

Purchase price adjustments.–As indicated, we have found that adjustments would increase the purchase price by $9.5 million. Such amount supplements the price Penn-Central will have to pay.

Side track refunds.–The amount of $600,000 claimed by Penn-Central appears to represent obligations of NH to shippers who advanced money for the construction of side tracks pursuant to agreements under which NH would reimburse them based upon the amount of traffic over those side tracks. While Penn-Central would assume these obligations, they are clearly of a contingent nature which may never require payment. In view of the nature of the item and the relatively small amount involved, we shall not take it into account as an item of cost to Penn-Central.

Freight losses.–The purchase agreement provides that Penn-Central would underwrite deficits in NH's net railway freight operating income for the years 1965–67, to a maximum of $1.75

million per year. It is undisputed that Penn-Central's liability would be $5.2 million, the maximum allowable during such period.

The Committee argues that this item should be disallowed because, under the agreement, it is taken into account in the final purchase price adjustments, and, therefore, should not be recognized as an item of cost in two separate places. Chase makes the same claim and effects a cancellation by including the amount among the purchase price adjustments it would omit. The record shows that the freight deficits are included in the $9.5 million which we have allowed for purchase price adjustments. Their retention as a separate item would manifestly be a duplication.

Labor protection and pension costs.—The Committee contends that the $19 million claimed by Penn-Central are not relevant to the purchase price because they will be incurred by Penn-Central, if at all, in the operation of NH and there will be offsetting revenues. In any event, it claims that the costs will be spread over a number of years and should be discounted to present value. Moreover, the Committee avers that these costs are deductible business operating expenses and must be further written down to the extent they reduce Penn-Central's income tax obligations.

Chase argues that the entire amount should be excluded because NH is under no legal obligation for such costs if it should be liquidated, and Penn-Central have deliberately assumed these costs in order to gain labor support for the Penn-Central merger.

The inquiry at the moment runs to Penn-Central's costs, not benefits. The latter have been analyzed in this report under a different heading. Regardless of the benefits or considerations flowing to Penn-Central or of the obligations NH might incur or escape in a real liquidation, the costs of Penn-Central in effecting NH's inclusion accrue inexorably. Penn-Central will incur a labor cost by virtue of the inclusion which they would not incur absent the inclusion. That cost is $19 million. If that amount can be attenuated or offset by factors not accounted for elsewhere in the analysis, they should be considered here. Penn-Central concede that a $5 million offset lies in the operational savings attainable from the reduction of personnel under unified operations. Whether and how an income tax deduction would materialize is subject to numerous variables; nevertheless, we believe it can be safely estimated that taking this item of cost as an income tax deduction would result in lowering the tax by more than $4.5 million (assuming the 24 percent effective tax rate claimed by Penn-Central). Employee good will and cooperation, undoubtedly

beneficial to Penn-Central, do not directly reduce this item of cost. However, they are factors of value, though intangible, which are translatable into operating savings. As such, they should be given weight in this computation. Considering the several pertinent factors, including the fact that a portion of the annual operating savings can be attributed to employee morale and good will, we conclude that the net cost to Penn-Central of the labor protection would be about $9 million.

Leased lines rental capitalized.– Penn-Central propose to assume NH's obligations under the latter's leases with the Holyoke and Westfield Railroad Company and the Norwich & Worcester Railroad. They have capitalized, as a cost of acquiring NH, that portion of the rentals which they believe would have to be disbursed to extinguish the lease liabilities. The amount claimed is $5.3 million. This item is disallowed. There is no evidence that Penn-Central will or is even likely to incur such a cost. It is clearly a hypothetical item.

Depreciation for 1964-66.–Since the purchase agreement does not provide for any reduction in price attributable to depreciation after December 31, 1963,[26] Penn-Central claim that the depreciation charged by NH since that date, $26.4 million, represents an item of cost to Penn-Central.

This claim is rejected. While depreciation—which is a measure of the consumption of assets—does relate directly to the value of the consideration flowing *to* Penn-Central, it is not pertinent to our immediate inquiry, which is to evaluate the consideration flowing *from* Penn-Central in terms of Penn-Central cost. The NH trustees appraised NH properties as of December 31, 1965, and we have adjusted our valuation results to December 31, 1966. Therefore, to the extent of its relevance, viz, in evaluating the properties Penn-Central would receive, depreciation since December 31, 1963, has been taken into account.

Deferred maintenance.– Penn-Central assert they will spend $32 million on NH properties for deferred maintenance. They do not sustain this claimed cost, since their testimony shows that the level of track maintenance on the NH is generally comparable to that on other class I roads with similar traffic volumes. There is considerable deferred maintenance on structures, primarily bridges, but no distinction is made between amounts expended normally to maintain these bridges and amounts claimed as deferred maintenance. They concede that it is safe to operate

[26]Except for property acquired after December 31, 1964.

over the bridges insofar as the NH equipment is concerned. The physical condition of the bridges was taken into account in their valuation.[27] Improvements to their condition should produce savings in operating costs and generate more revenues. *N&W Inclusion* case, *supra*, at pages 809–810. In these circumstances, allowance of deferred maintenance as a cost to Penn-Central cannot be upheld.

Assets purchased.—The purchase agreement provides for closing adjustments other than purchase price adjustments. Basically, under this provision, Penn-Central would acquire certain of NH current assets and assume its current liabilities. The purpose of this provision is to take care of the mechanics of ending NH's railroad operations. The theory of this provision is the Penn-Central will pay the trustees an amount equal to NH's current assets other than cash and the trustees will pay Penn-Central an amount equal to NH's current liabilities plus $1 million.

The reason for the $1 million payment to Penn-Central is to account in part for the experience of all railroads that their book assets are subject to some discount by reason of poor credit risks, bankruptcy and other similar factors, whereas their book liabilities are generally required to be paid in full. If a procedure of this kind were not agreed upon the trustees could anticipate continued employment of a large staff. From their point of view, this staff would cost considerably more than the payment of $1 million to Penn-Central for winding up NH affairs. From the point of view of Penn-Central, these accounts are of a permanent nature and their immediate takeover is of sufficient advantage to them to permit their sharing with the trustees the costs otherwise attributable to winding up NH accounts.

If the transaction had been consummated as of October 31, 1966, the total assets to be sold to Penn-Central under this provision would have amounted to $11.6 million, and Penn-Central would have assumed $20.9 million in liabilities. The net result of these adjustments plus the payment of $1 million would have resulted in an obligation of the NH trustees to pay $10.3 million to Penn-Central.

Penn-Central claim that the $11.6 million in assets to be acquired constituted a cost of the transaction to them. This contention is without foundation since the adjustments balance out. There is no gain or loss to Penn-Central. Accordingly, we reject the Penn-Central claim.

[27] This is true also with respect to ways and structures.

Cost of NH assets to Penn-Central.–Based on the foregoing, we find that the cost to Penn-Central of acquiring the NH assets is around $159 million.

SUMMARY AND CONCLUSIONS CONCERNING VALUE OF NH AND REASONABLENESS OF CONSIDERATION

The total value of assets shown on NH's balance sheet as of October 31, 1966, is $384 million. However, few parties even claim that the value of NH assets for purposes of this proceeding should be determined by their book value. Rather, all have emphasized the appraised values of the assets.

We have already determined that inclusion of NH's operations in Penn-Central will be consistent with the public interest and have so conditioned our approval of the merger. Even though inclusion of NH in the merger is required, nevertheless, we are considering both the fair upset price of the property as contemplated by section 77 of the Bankruptcy Act and also how much the NH creditors might realize in a liquidation. Liquidation value as used by both the NH trustees and Penn-Central is the estimated market value that would be realized in a total liquidation, less the cost of dismantling properties and other liquidation costs and after discounting proceeds to present worth.

As detailed earlier, we have found the liquidation value of NH to be $125 million. We have also found that the value to NH of the consideration to be received is $125 million. It is evident, therefore, that the consideration is at least equivalent to the liquidation value and will, therefore, be equitable to all parties having an interest in the NH estate to approve the transaction.

From the point of view of Penn-Central, we have found that the total cost to them of acquiring the assets is $159 million. In these circumstances, it would be unfair to Penn-Central to require them to pay a price greater than that agreed upon in the purchase agreement.

Penn-Central must assume a loss-operation which not merely lacks promise of foreseeable recovery, but in fact is plagued by an unrelenting erosion. Thus, they are faced with constantly diminishing going concern values. The cold, hard fact is that NH has been losing money for years and that unfortunate situation continues unarrested. As thorough as may be the analyses forecasting profitable operations for NH as a freight-only railroad, they are subject to the fulfillment of a number of conditions and

the achievement of proposals as yet untested by experience. We cannot give such projections as much weight as the actual operating results of many years.

The Committee contends that NH must receive a consideration which would yield to the creditors what they would have obtained if operations had ceased on December 31, 1963, when the trustees concluded NH could not be reorganized short of inclusion in a major trunkline system.

The Committee fails in this contention because it produced no evidence as to what the creditors would have obtained on December 31, 1963. We cannot conclude on this record that the NH would have derived a liquidation value different from that determined herein. Moreover, the Committee has not established how a decision of the NH trustee, and the timing thereof, could determine what would be a fair consideration for Penn-Central to pay.

Penn-Central ask that an allowance be made to the earliest date at which a liquidation could reasonably be anticipated for the constant diminution of NH's assets. The request is denied. As we indicated earlier herein, a large portion of NH assets consists of land. We cannot assume that these values will diminish. It is at least as reasonable to presuppose that the values will increase. Moreover, we have given weight to the NH's operating losses and the prospect that they may continue in determining the consideration to be paid by Penn-Central.[28]

Manufacturers ask that Penn stock to be delivered to NH be valued at its average market price for the last trading day of each month of a period at least 6 months prior to the date of our decision. Chase makes a similar request, suggesting that the value of Penn stock be set at the average of the closing prices of Penn stock at the end of each of the first 6 months of 1967.

The suggested approaches are not appropriate in this case. The stock is the most volatile of all the properties valued herein. The market price of Penn stock has trended upward since 1962 from a mean price of $14.50 per share in that year to a mean price of almost $57.11 for 1966. We believe that use of the suggested periods would understate the value of the stock to be paid to NH. We are satisfied that our estimate of a value of $87.50 on the Penn stock fairly reflects the inherent qualities of the stock. Accordingly, we deny the requests of Manufacturers and Chase.

[28] The financial terms are subject to adjustment in accordance with the provisions of item 12 of the first "appearing" paragraph (page 3) of our order of August 1, 1967.

Gruss asks that NH's first mortgage bondholders be compensated in long-term callable subordinated convertible debentures of Penn-Central bearing interest at a rate sufficient to maintain a value approximating their principal amount and a conversion price reflecting reasonable prospects of market value of the stock.

The request is denied. The NH's first mortgage bondholders invested in a security, the principal amount of which is in jeopardy and which produces no return for them.[29] Gruss would take advantage of the inclusion to turn the adversity of the first mortgage bondholders into a successful investment. Not only would they obtain the protection and security afforded by holding an interest paying debenture of Penn-Central, but they would also have the choice of gaining the substantial benefits of an equity holder if the promise of the Penn-Central merger should be realized. Nothing in this record justifies placing NH's first mortgage bondholders in such a favored position.

INTERIM SUPPORT

We turn now to the matter of support of the NH operations until the NH assets can be conveyed to Penn-Central. Chase raises a threshold issue. It argues that we have no power to hold a hearing which involves the issuance of trustees' certificates inasmuch as the reorganization court has not authorized the NH trustees to issue such certificates. Chase claims that section 77(c)(3) of the Bankruptcy Act does not contemplate that the Commission will act on the matter of trustees' certificates before publication by the court has been completed, a hearing held in the court, and a determination made by the court.

We find no merit in this contention; section 77(c)(3) does not preclude action by the Commission prior to NH's obtaining court approval. The Commission has jurisdiction under section 5(2) of the Interstate Commerce Act to hold hearings which, among other things, concern just and reasonable terms and conditions for approving and authorizing a proposed transaction under that section, in this case the merger of Central into Penn. It is pursuant to such authority that the hearing on interim support for the NH has been held. This does not impair the jurisdiction of the reorganization court in any way, for our authorization does not relieve the NH trustees from obtaining any necessary approval of the reorganization court for the issuance of trustees' cer-

[29] See appendix H for interest in default.

tificates. For example, the Commission's order of August 2, 1961, in Finance Docket No. 21685, et al., *New York New Haven & Hartford Railroad Company Trustees' Loan Guaranty*, authorizing the NH trustees to issue $5 million in trustees' certificates to evidence and secure a long guaranty under the then effective part V of the Interstate Commerce Act, was issued prior to order No. 4 of the reorganization court authorizing the borrowing and issuance of the trustees' certificates, and such action was noted in the court's order.

To place the merits of the matter in context, it is helpful to stress again the significance of the NH's operations. In our decision in the *NH Train Discontinuance* case, 327 I.C.C. at page 224, we found, "The record fully demonstrates that New Haven's passenger service is an essential component of the commerce of New England." The essential nature of the NH's operations is epitomized by our finding in the instant proceeding that the Penn-Central merger "without complete inclusion of NH, would not be consistent with the public interest, and, accordingly, we will require all the New Haven railroad to be included in the applicants' transaction." 327 I.C.C. at page 524. Again, on reconsideration, we referred to the NH's "vital passenger and freight operations." 328 I.C.C. at page 312. In view of these findings and as the agency entrusted with and responsible for "developing, coordinating, and preserving a national transportation system by water, highway, and rail, as well as other means, adequate to meet the needs of the commerce of the United States, of the Postal Service, and of the national defense,"[30] our efforts necessarily must be directed towards assuring the continuation of the NH's railroad services.

Inclusion of NH as condition precedent to Penn-Central merger.—Gruss contends that we ignored the issues regarding inclusion of the NH simultaneously with consummation of the Penn-Central merger when we said in our September 12, 1967, order, on page 2, that "consummation of the Penn-Central merger should proceed pending such determination of appropriate means for interim support of the NH." Such is not the case. We had several times previously concluded on the basis of the record that delay of the Penn-Central merger until inclusion of the NH can take place is not warranted. 327 I.C.C. at page 527; 328 I.C.C. at page 306; 330 I.C.C. at page 361. Clearly, no prejudgment was involved.

[30] National transportation policy, 54 Stat. 899. See also *Ecker v. Western Pacific R. Corp.*, 318 U.S. 448, 482 (1943), wherein the court emphasized that "the interest of the public is an adequate transportation service must receive consideration."

Instead, the September 12 order was completely in accord with our prior rulings. Gruss' request for withdrawal of the "prejudging recital" is denied.

Need for immediate action.–Shapp challenges the existence of the asserted emergency. He contends that the NH's claimed need is based on a forecast which is subject to correction or adjustment and that the NH has already revised the earlier estimate set forth in our order of August 1, 1967, that the NH would be unable to meet its payroll by September 1, 1967.

The evidence of the NH's cash requirements submitted by the NH trustees at the September 1967 hearing is the most current evidence of record on this point. Of all the parties, only Shapp questions its reliability, and Shapp did not cross-examine the sponsoring witness. True, like all data dealing with the future, it is a forecast. However, the witness was fully competent to make such an estimate. If we were to accept Shapp's position, we could not receive evidence dealing with anticipated occurrences and the regulatory process would become impotent. The evidence indicates that the NH will need cash assistance in January 1968. To avoid the collapse of the NH's operations, action must be taken now. We would be remiss in our responsibilities to the public if we waited until the actual cessation of operations to institute measures to help the NH, measures which by that time undoubtedly would be "too little and too late." We find Shapp's contention without substance.

Effectiveness of lease or loan.–Chase contends that the proposals do not meet the need to give prompt financial assistance to the NH because they are predicated on consummation of the Penn-Central merger and it is unrealistic to expect that the merger will take place by January 1968. In lieu thereof, Chase recommends that the NH trustees renew their application for discontinuance of passenger service unless the public authorities agree to pay an adequate subsidy. In this connection, they ask us to refrain from holding a hearing and to permit the discontinuance to take place 30 days after filing of the notice of intent to discontinue.

There is no gainsaying that consummation of the Penn-Central merger is prerequisite to furnishing the NH aid under the proposed loan arrangement; and our decision herein is based on the assumption that there will be a timely Penn-Central merger.

In any event, the course of action espoused by Chase is even less likely to produce timely and adequate aid for the NH. The essential character of the NH's passenger service renders it

extremely doubtful that our responsibilities under section 13a of the Interstate Commerce Act would allow us to permit a complete cessation of passenger operations, and certainly we could not countenance such a result without a full public hearing. Moreover, insofar as implementation of our decision in the *NH Train Discontinuance* case, *supra*, is concerned, the proposal in this regard filed by the NH trustees in Finance Docket No. 24628, and later withdrawn, anticipated net annual savings of $314,000, including a noncash expense of $84,000 in equipment depreciation, hardly sufficient to provide the NH with the level of help the instant record shows it requires.[31]

We are convinced, therefore, that the approach reflected in our order of August 1, as amended September 12, offers the greatest possibility of successfully shoring up the NH's financial position pending transfer of its assets to the ownership of Penn-Central.

Lease versus loan.—To the NH trustees, a lease by Penn-Central would be a sound means of sustaining the NH's operations until the NH could be physically included in Penn-Central. However, their problem with a lease is one of practicability in the time available. They believe that, at best, it would take 4 to 6 months to prepare a lease and that, with the litigation that would probably be required for its approval, it would be impossible to implement a lease before the NH's operations had stopped.

Penn and Central assert that at least a year would be required to put a lease into effect. In addition, they object to a lease because they contend that Penn-Central could not effect economies under a temporary lease, but, instead, would suffer increased costs arising from labor protective conditions.

Accordingly, the NH trustees and Penn and Central have advanced loan proposals as the basis for interim support of the NH's operations.

The States and NH creditor groups disagree with the NH trustees and Penn and Central about the difficulties and amount of time involved in preparing and implementing a lease. These parties argue that a lease is not only feasible but also has clearcut advantages over a loan arrangement. They contend that a lease arrangement is necessary in order that economies and efficiencies in operations be effected immediately. Connecticut and New York assert that a prompt takeover of the NH's operations

[31] Savings of $314,000 would be realized over the year and not instantly.

by Penn-Central is necessary to advance their program to revitalize the west-end commuter service. Creditor groups urge that they have borne the NH's losses long enough and that it would be an improper taking of their property prohibited by the Constitution if they are required to continue to bear such losses.[32]

Though in our order of August 1 a lease agreement was specified, we were seeking the most appropriate means of assuring the continuation of the NH's operations, an equitable distribution of the continuing burdens of those operations, and the effectuation of measures to minimize operating losses without curtailment of essential services. Based on the record made at the September 1967 hearing and the arguments of the parties, we are persuaded that a loan arrangement affords the most suitable instrument to accomplish these objectives.

The evidence establishes that a $25-million loan over a period of 3 years should enable the NH to sustain its operations until its assets are conveyed to Penn-Central. Moreover, we can provide for an equitable distribution of the burdens of the operations as effectively under a loan arrangement as under a lease. Under all the circumstances presented, operational economies would not be more feasible under a lease than under a loan arrangement. Penn-Central obviously would be hesitant to make capital expenditures for improvement of NH facilities, or to take steps to integrate the NH's operations into their own, until the matter of including the NH in their system was completely resolved. Nor does it follow that a lease, more so than a loan arrangement, would facilitate the program of the States of Connecticut and New York to take over and improve the commuter service into and out of New York City.

The creditors argue strenuously that their property would be taken without due process unless they no longer have to absorb the NH's operating losses.[33] The Committee maintains that even

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[32] Gruss requests us to reverse the ruling of the hearing examiner rejecting admission of an exhibit consisting of a pro forma balance sheet of the NH as of June 30, 1967, giving effect to acquisition of the B&P properties and consummation of the purchase agreement with Penn-Central. The request is denied. The exhibit updates data which were submitted at the hearings that closed in May. It was made clear in our order of August 1 that the proceedings instituted by that order were for a limited purpose and did not constitute a blanket reopening of the record. The examiner's ruling rejecting the proffered evidence properly reflected the scope of the hearing before him.

[33] To speak only of the NH's "operating losses" obscures the matter. The interests of the NH bondholders stem primarily from their liens on the NH assets. Losses which reduce the value of the assets or represent deferral of expenses

(footnote 33 continued on next page)

the trustees' proposal to have Penn-Central take over losses is unacceptable because, if the creditors vote against the plan of reorganization, all the losses would fall upon them.

These contentions are unimpressive. We have found herein the fair liquidation value of the NH properties and that the consideration to be paid by Penn-Central is worth at least that value. We know of no legal requirement that would compel Penn-Central to protect the NH estate against diminution in value until the assets can be transferred to them.[34] If the creditors believe that it is to their advantage to have the reorganization proceeding dismissed and the NH liquidated in an equity proceeding, it is manifest that, unless the States were induced to maintain and, in fact, increase their aid, the creditors might well have to carry the NH's operating losses until those proceedings were completed and the NH were allowed to abandon its operations, even assuming the NH's creditors' position were sustained by the reorganization court and this Commission. It is clear to us from the record that the NH's creditors would not gain from such a procedure.

The creditors also protest that their interests will be reduced by the issuance of trustees' certificates which will have precedence over their claims against the NH estate. We consider such a result part of the process of distributing the burdens of the NH's operations. It is a fundamental aspect of our free enterprise economy that private persons assume the risks attached to their investments, and the NH creditors can expect no less because the NH's properties are devoted to a public use. Indeed, the assistance the creditors are receiving from the States and would receive from Penn-Central through the sharing of operating losses would raise some of that burden from their shoulders.

(footnote 33 continued)
that have a prior claim on the NH estate weaken the interests of these creditors. Thus, the creditors are hurt when cash expenses exceed cash income resulting in an attrition of the current assets available to pay priority claims on the estate and by the deferral of payment of real estate taxes, per diem charges in dispute, and tort claim liabilities having the status of administrative expenses. Noncash operating items, such as depreciation charges and retirement losses, do not diminish the interest of the creditors in the NH estate. Furthermore, under the purchase agreement, except to a limited extent, charges for depreciation do not serve to reduce the purchase price.

[34] This is apart from any consideration as to whether it would be fair and reasonable, in all the circumstances, to require Penn-Central to share in the burden of the NH's operating losses.

We can devote little consideration to the lease proposals of Manufacturers and Gruss. They were advanced in briefs and were not supported by any witness. In its brief of July 17, Manufacturers concedes that it does not have sufficient familiarity with the NH's operations to formulate detailed proposals as to the form and content of a lease. Gruss also admits, in his brief of October 12, that his proposal is incomplete.

Those who seek a lease are, for the most part, looking for a quick way to transfer the burden of this deficit operation to Penn-Central, and not only for a means of preserving the continuity of NH service. Like Judge Anderson in his memorandum of July 11, 1967,[35] we recognize the patent unfairness of any plan which shifts the burden to Penn-Central and thereby relieves the creditors and the affected governmental entities and allows creditors to litigate at length the value and relative rank of their interests, but does not accord Penn-Central the power to manage and dispose of the properties as owner. Our order of August 1, 1967, calling for a lease contemplated that the deficit during the lease period would be shared by the NH, Penn-Central and the States. The lease terms proposed by Manufacturers and Gruss do not provide for this sharing of the interim deficit, but instead would totally relieve the creditors of any burden.

The only reason we considered a lease was to permit a quick takeover of NH operations by Penn-Central, because NH lacks sufficient funds and other resources to continue operations while reorganization proceeds. The quick takeover would serve the public interest in a number of ways: most important it would prevent an NH shutdown and preserve NH service which we have found essential; it would free the NH from the uncompromising shackles of abject poverty which have kept NH service in a steady decline, and would open the way to integration of the NH operations into an enlarged, modernized rail system under proven rail management; it would at least slacken the erosion of the NH asset value to the extent Penn-Central would share in the burden of a Penn-Central takeover with the character of permanence which would facilitate the attainment of these objectives. The record now convinces us that a quick takeover in this case could not be accomplished by means of a lease.

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[35] Noting NH's rapid cash attrition, the bankruptcy court, U. S. District Court for the District of Connecticut, suggested that this Commission consider means, by lease or other method, for an assumption of the NH operations by Penn-Central immediately upon consummation of their merger.

The lease of an entire railroad by a prospective purchaser as a preliminary to the purchase is unusual. It creates undue complications, for practically all the elements that go into a decision on a purchase, *e.g.*, all the specified criteria of section 5(2), must be considered, plus the additional factors that arise in contemplating a possible reversion to the lessor—in this case, a bankrupt on the verge of liquidation. To plan, weigh and litigate a just and suitable lease takes time, an essential constituent not here available, if the NH is to receive from Penn-Central the financial stimulant so urgently needed.

We believe that, short of an immediate takeover of NH operations, the interim support loan for which we are here prescribing terms will assure continuity of NH service and best serve the public interest. At the same time, our concurrent approval of the "first step" of the trustees' general proposal for a plan of reorganization—the sale of the NH assets to Penn-Central—will facilitate the quick and absolute takeover of the NH operations that the public and private interests, properly weighed, require.

Loan provisions.—Briefly summarizing, both loan proposals provide for an aggregate principal amount not exceeding $25 million to be taken down as needed over a period of 3 years, beginning with the consummation of the Penn-Central merger, in amounts governed by formulae tied to the NH's cash balance. The $25 million is considered by the NH trustees as an outside protective figure and they believe the NH's cash loss over the 3-year period would be considerably less than that amount. Moreover, they assume that the Penn-Central merger will become effective in the very near future and hope that the NH will be included in the new system within a year after consummation of the merger. Among the conditions to each loan is the requirement that the assistance now being received by the NH from public bodies be continued in effect.

Each loan takedown would be evidenced by a trustees' certificate which would be on a parity with the NH trustees' certificates presently outstanding and would represent an administration claim against the NH estate. As such, the trustees' certificates to be issued to Penn-Central would constitute a charge and direct first lien upon all property and earnings of the NH estate prior in right to the liens, among others, of all mortgages. The NH trustees propose a form of trustees' certificate patterned after the outstanding certificates to the extent applicable.

In general we find the loan and trustees' certificate provisions proposed by the NH trustees fair and reasonable and approve them as the basis for agreement between the trustees and Penn and Central except insofar as modified hereinafter. Those provisions which warrant comment are discussed below.

Limitation on annual amount of loans.—Both proposals provide for a maximum loan of $25 million. However, the proposal of the NH trustees does not provide for annual limits on the takedown while Penn and Central propose a limit of $7 million in the first year, $8.5 million in the second year, and $9.5 million in the third year.

The trustees believe that the imposition of yearly limitations on the amount that can be borrowed could frustrate the whole purpose of the loan agreement and is unnecessary to protect Penn-Central in view of the safeguards existing in their proposed form of loan agreement. Penn and Central consider the annual limits important, contending that (1) they would impose a requirement of greater efficiency on the part of the NH management than if the full $25 million were immediately available; (2) they would help insure that the $25 million would cover the entire 3-year period; (3) if the annual limits were not sufficient, it would be because the NH losses had greatly accelerated and in that case Penn-Central wants the opportunity to review with the States their participation in the loss; and (4) the availability of $25 million would be an invitation to the States to discontinue their aid.

The imposition of annual limits on the loan is not acceptable. The dominant consideration is the continuation of the NH's services, and if that were gravely threatened we could not allow the artificial barriers Penn-Central would lay down to obstruct needed help for the NH. It is not apparent why the availability of the $25 million immediately would induce the NH's management to make uneconomical expenditures or to conduct operations inefficiently. In any event, the limitations on the amount that can be borrowed at any one time and the requirement for a 3-month interval between loan takedowns, discussed hereinafter, furnish sufficient protection against the NH's drawing sums greater than its needs. Other provisions in the loan agreement and in the operating loss formula supply ample protection against a substantial reduction in State aid.

Amount of individual takedown.—Under the proposal of the NH trustees any time the cash balance falls below $5 million they

may borrow the amount necessary to equal $5 million plus $2.5 million. The latter amount is to cover the additional cash attrition which may occur before the loan is actually taken down.

The Penn-Central proposal provides that when the NH cash balance drops under $5 million, the NH may borrow enough money to raise the cash balance to $6 million.

We believe the larger loan amounts suggested by the NH trustees are preferable, particularly since we will impose the 3-months interval between loans advocated by Penn-Central. There is a danger that under the limitations Penn-Central propose the NH trustees might find themselves without sufficient cash to carry on and be unable to borrow more funds from Penn-Central because of the 3-month time interval condition.

Interval between loans.—The NH trustees and Penn-Central propose that 30 days' notice be given before the drawdown of an amount under the loan arrangement. In addition, the latter request an interval of at least 3 months between loan takedowns. The principal reason for the 3-month interval is to assist Penn-Central's own fiscal planning and to avoid the necessity of Penn-Central keeping an extra cash balance for the NH to tap at any time. The NH trustees concede that the 90-day period between loans is not in itself unduly burdensome but fear that it could interfere with orderly operations because of the other conditions Penn-Central would place on the trustees' ability to anticipate cash requirements.

The proposal of Penn-Central is reasonable and will be adopted. The record indicates that the NH can exist on relatively small amounts of cash and that it should have no difficulty in anticipating its cash needs within a 3-months limitation. It is appropriate to take Penn-Central's fiscal requirements into account in determining equitable terms for the loan arrangement. This will place no undue burden on the NH inasmuch as we are not adopting Penn-Central's other proposals affecting loan takedowns.

Date of cash balance.—Both proposals provide that a notice requesting a loan be accompanied by a closing certificate setting forth the NH's cash balance. Under the NH trustees' proposal, the certificate may have any date on which the trustees desire to set the notice machinery into motion. Penn-Central would require the certificate to be dated as of the last day of the month preceding the month in which the notice is given.

The NH trustees point out that, if the NH's cash balance at the end of a month should be slightly greater than $5 million, the

Penn-Central proposal would prevent the trustees from borrowing during the subsequent month although the cash drain during that month might be substantial. Thus, they might be unable to obtain timely aid from Penn-Central. Moreover, it does not appear that the Penn-Central proposal involves any important protection for themselves. Accordingly, we reject the Penn-Central provisions.

Computation of NH cash balance.–The proposals of the NH trustees and Penn-Central provide that the cash balance of the NH include cash and temporary cash investments, accounts Nos. 701 and 702, respectively, of our Uniform System of Accounts for Railroad Companies. The NH trustees stress, however, that reserves to account for amounts withheld from employees for Federal income and railroad retirement taxes, normally held in the form of temporary cash investments reflected in account No. 702, should be excluded from the cash balance computation. Penn-Central agreed to this treatment.

Penn-Central would include two other items in the cash balance. The first is unexpended proceeds of trustees' certificates not reflected in accounts Nos. 701 and 702. The NH trustees have no objection to including this item in computing the NH's cash balance. The second of these items is any expenditure incident to transactions requiring the joint approval of Penn and Central under section 14 of the purchase agreement and not so approved. In this regard, Penn-Central aver that they should not be obligated to lend money to the NH trustees to pay for capital improvements which Penn-Central do not approve.

This proposal is rejected. The NH trustees still have the responsibility of operating that railroad. We do not believe it appropriate to afford Penn-Central this means of indirectly controlling the expenditures the NH would make.

In summary, we approve the provisions with respect to computation of the NH's cash balance to the extent agreed upon between the NH trustees and Penn-Central.

Penn-Central audit of NH's cash balance.–Penn-Central request that, as a condition to closing each loan takedown sought by the NH trustees, the latter be required to provide such information as Penn-Central may reasonably request in order to enable Penn-Central to ascertain the accuracy of the computation of the NH's cash balance.

We see no warrant in such a provision. It could act to delay the furnishing of desperately needed funds and jeopardize the

performance of service by the NH. Under the NH trustees' proposal, each request for a loan would be accompanied by the NH's treasurer's certificate setting forth the amount by which the cash balance is less than $5 million. This is a sufficient safeguard against unjustified loan requests.

Effect of reduction in State aid.—The NH trustees contend that any reduction in State aid should correspondingly reduce the amount that can be borrowed from Penn-Central. The latter propose that a reduction in State aid of more than $200,000 would be a reason for terminating Penn-Central's obligation to lend money to the NH.

Both proposals are manifestly directed at dissuading the States from reducing the assistance rendered the NH because of the financial support available from Penn-Central. We shall adopt the proposal of the NH trustees. That of Penn-Central is too drastic. It ignores the circumstances under which the State aid might be reduced and might cause the cessation of the NH operations unnecessarily. All interested parties—the States, Penn-Central, and the NH creditors—must cooperate if the NH operations are to continue until the NH is finally included in the Penn-Central system. But it is not for Penn-Central to determine unilaterally the extent of the assistance they and the other interested parties shall render the NH. Penn-Central cannot eschew the responsibilities they have under just and reasonable terms and conditions for approval of their merger by claiming that some other party is delinquent on its part. No automatic formula such as Penn-Central propose can be allowed to determine what is consistent with the public interest.

Measurement of State aid.—Under the NH proposal, the State aid would be measured by the amount received by the NH in 1967. If any State were to reduce its aid, another State could make up the difference. Payments from the Massachusetts Bay Transportation Authority (MBTA) are considered by the trustees to be compensation for the performance of certain passenger service rather than State aid. The trustees propose that if all, or a portion, of the payments from the MBTA should cease, the amount of the loan takedowns be unaffected as long as the NH terminates the passenger service relating to such payments as authorized in *New York, N. H. & H. R. Co. Discontinuance of Service*, 327 I.C.C. 77 (1965).

Penn-Central would utilize the level of State aid as of September 1, 1967. However, each State or authority would be required to

continue aid at its level on that date without regard to the payments of the other States or authorities. The trustees' agreement with the MBTA is treated as an aid program.

The NH trustees state that the level of State aid at September 1, 1967, may properly be adopted and we agree with that position. The current level of State aid is more indicative of the NH's needs. Unless there should be a significant reduction in the NH's services, there appears no satisfactory reason why the present level of State aid should not be maintained. It is, therefore, the appropriate measure to be employed.

For reasons given in the preceding section on the effect of a reduction in State aid, we reject the other aspects of the Penn-Central proposal with respect to the level of State aid and accept the recommendations of the NH trustees in this regard.

The States are disturbed by the loan provisions which, on the one hand, appear to contemplate possible reductions of service by the NH, as hereinafter discussed, and, on the other hand, maintenance of current levels of State aid. However, our evaluation of any abandonment or train discontinuance proposal would take into account the effect on the amount of State aid. There should be no concern that the approval of an abandonment or train discontinuance proposal would result either in the States being unfairly held to levels of aid which are not commensurate with the service being provided or with the NH finding itself with insufficient funds to carry on its operations.[36]

Interest.– The NH trustees suggest an interest rate of 5 percent. Penn-Central request the prime rate of the Morgan Guaranty Trust Company of New York City at the time the loan is taken down. They contend that this assures the NH of the best prevailing market price of money and that Penn-Central themselves may not be able to borrow the money necessary to make the loans at the prime rate.

We think that considerations of equality of treatment require that the interest rate shall be the prime rate of the Morgan Guaranty Trust Company at the time the loan is taken down.

[36] Manufacturers asserts our August 1 order erred in indicating implicitly that the current level of State support for the NH's operations is an adequate discharge of the States' responsibility to the public. The reference in our order to lease terms which would equitably distribute the burden of the NH's operating deficits including provisions for "contributions by the involved States at no less than present levels" (page 3 of order) in no way constituted a judgment of the adequacy or inadequacy of State aid. It merely took into account the prevailing situation.

Maturity of trustees' certificates.—The NH trustees propose that the trustees' certificates to be issued as evidence of the loans to be made by Penn-Central mature 31/2 years after the date of the Penn-Central merger. Penn-Central suggest that the maturity date be December 13, 1971, the same maturity date as the latest of the NH's currently outstanding trustees' certificates.

There is little to choose between the two proposals. In their brief, the NH trustees state that they have no objection to Penn-Central's proposal. Accordingly, we accept December 13, 1971, as the maturity date for the trustees' certificates.

Repayment.—The matter of handling the repayment of the loan to the NH is dealt with hereinafter in connection with the discussion on absorbing operating losses.

Cost of trustees' certificates.—Penn-Central would have the NH trustees pay all the costs attributable to the trustees' certificates including those incurred by Penn-Central. They contend that this is a normal provision in loan transactions and is contained in the other certificates issued by the trustees. The NH trustees maintain that each party should cover its own costs.

We are here concerned with an equitable sharing of the burdens of operating the NH until it can be included in the Penn-Central system. Moreover, obviously the NH bears a very special relationship to Penn-Central. In these circumstances, whatever the customary provisions regarding loan costs may be, we are satisfied that the proposal of the NH trustees represents a fair handling of this matter.

Abandonments and train discontinuances.—The NH trustees and Penn-Central would confer on the latter the right to designate lines to be abandoned[37] and train service to be discontinued. Penn-Central also ask the right to specify station and terminal operations to be ended. The NH trustees would have Penn-Central pay the costs of such proceedings; Penn-Central contend that the costs of the proceedings should be an obligation of the NH.

As the NH trustees interpret their proposal, although they would be required to institute an abandonment or train discontinuance proceeding if requested by Penn-Central, even if the application should be granted the decision as to whether the abandonment or train discontinuance actually takes place would

[37] Section 14.1.10 of the purchase agreement makes any application by the NH for authority to abandon operations over a line of railroad subject to the joint approval of Penn and Central.

rest with the NH trustees. Penn-Central state that, as a practical matter, they would not insist on the initiation of abandonment or train discontinuance proceedings if the NH trustees did not agree with their proposal.

The problems raised concerning abandonments and train discontinuances are directly related to the broader matter of efficiencies and economies in the NH's operations. Inasmuch as we have hereinafter decided that Penn-Central will share in the operating losses of the NH, they should have a voice in the imposition of economies and efficiencies in its operations. In this connection, the NH trustees have made known their willingness to establish a joint advisory committee. Penn-Central declare they are completely opposed to such an arrangement on the grounds that it is ineffective and might possibly open Penn-Central to litigation by dissatisfied creditors of the NH. Penn-Central's contentions are unpersuasive. These same arguments appear just as applicable to the Penn-Central proposal that they be given the right to prescribe lines to be abandoned, trains to be discontinued, and station and terminal operations to be halted. Moreover, Penn and Central now have an important role with respect to transactions of the NH through the functions of the approval committee under section 14 of the purchase agreement. We think it desirable that Penn and Central reconsider their position as regards the joint advisory committee.

In any event, the ultimate responsibility for the NH's operations remains with the NH trustees until the NH is included in the Penn-Central system. In these circumstances, it would be meaningless to bestow on Penn-Central the right to require the NH to embark on abandonment or train discontinuance proceedings when the conclusive decision must be that of the NH trustees. On this point, therefore, we disapprove the proposed loan agreement provisions.

Of course, as previously indicated, Penn-Central may recommend lines for abandonment and other economies and efficiencies in the NH's operations. The costs of processing abandonment and train discontinuance proceedings should be borne by the NH, however, as the responsibility for the NH operations is still carried by the NH trustees. Nevertheless, it should not be overlooked that the costs of these proceedings would be reflected in the operating results of the NH and that Penn-Central will share in the operating losses under the formula prescribed in a later section.

Events terminating obligation to loan.—Penn-Central request that the occurrence of any of eight events conclude their undertaking to lend money to the NH. These are as follows:

(1) Acquisition of the NH by Penn-Central;
(2) If State aid to the NH should be reduced more than $200,000 below the level at September 1, 1967;
(3) If the NH trustees request, or acquiesce in, liquidation of the NH properties or their disposition to someone other than Penn-Central;
(4) If a regulatory authority or court by a final and effective order grants permission to liquidate the NH or to dispose of it to someone other than Penn-Central;
(5) If the NH should cease to be operated as a going railroad;
(6) If it should be determined that Penn-Central shall not acquire the NH;
(7) If a default exists in any outstanding trustees' certificates; and
(8) Expiration of 3 years from the date of the Penn-Central merger.

Items (1), (4), (5), (6), and (8) constitute reasonable bases for ending Penn-Central's obligation to lend money to the NH. We have earlier rejected item (2) as a ground for closing Penn-Central's obligation, and no further discussion of that item is required here.

We also disapprove items (3) and (7) as grounds for terminating Penn-Central's responsibility. Until authority to liquidate or transfer the NH assets to someone other than Penn-Central is actually granted by the appropriate bodies, the obligation of Penn-Central to support the NH financially must survive so that the NH's operations can be maintained. This is because the mere request by the NH trustees for, or their acquiescence in, liquidation of the NH properties or their disposition to someone other than Penn-Central does not mean that such action will be permitted.

Similarly, the fact that a default may exist with respect to other outstanding trustees' certificates should not serve to relieve Penn-Central of their loan obligation. Such default may be waived by the person holding the other trustees' certificates or measures may be taken to overcome the default. In any event, continuation of the NH's operations may be feasible despite the default as long as loan support from Penn-Central is available. Therefore, absent a default in the trustees' certificates issued to Penn-Central, their obligation should continue.

Absorption of operating losses.—In all the circumstances we are convinced that, as an integral part of our approval of the terms of NH's inclusion under section 5(2), Penn-Central should share in the NH operating losses during the term of the loan

agreement. We have heretofore discussed the vital need for continuation of the NH's services and the importance of including the NH in the Penn-Central system as soon as possible. We believe that by requiring all interested parties to share in the operating losses of the NH during the interim period we can best accomplish our objective. If any of these parties should not cooperate during this period, the NH might be unable to continue service causing serious injury to the economy of New England, and, indeed, adverse effect on the affairs of the Nation as a whole. As we said in approving the Penn and Central merger (327 I.C.C. at 525), "Inclusion of the New Haven's services and the restructuring effort which we call for here and in our ultimate conclusions in the discontinuance case will not be easy. It will demand coordination, cooperation and statesmanship on the part of many interests involved as well as the railroads." This, of course, includes Penn-Central.

Penn and Central claim that imposition of the NH's operating losses on Penn-Central prior to the purchase of the NH's property would violate the standards of section 5(2)(b) of the Interstate Commerce Act that the terms and conditions prescribed by the Commission be "just and reasonable" and those of section 5(2)(d) that inclusion be on "equitable" terms. This contention is without substance. One of the conditions underlying our approval of the Penn-Central merger is the inclusion of the NH, and it contemplates the possibility of an immediate Penn-Central takeover of the NH operation with all its burdens. A requirement for partial support in the face of a postponed inclusion is less onerous and would, therefore, not be inequitable. Further, a responsibility for a share of the deficit during the interim period provides a safeguard against predatory competition with the NH and thereby relieves us of having to impose appendix G-type conditions.[38] A related consideration is that a requirement (on Penn-Central, the creditors and the States) to contribute to the interim deficit of an operation under trustee management should encourage all parties to shorten the litigation still before us in the NH inclusion and reorganization proceedings.

It is not unfair to Penn-Central to require them to share in the NH's operating losses pending their acquisition of the NH assets for other reasons. As Penn and Central have pointed out, under the purchase agreement they are absorbing up to $1.75

[38] Refer to appendix G of the prior report, in 327 I.C.C. 475 and revised in 330 I.C.C. 828.

million of the NH's freight deficit in each of the years 1965 through 1967. Moreover, Penn and Central contend that, to the extent the purchase agreement does not provide for a decrease in the purchase price for depreciation charged since 1963, Penn-Central will assimilate such costs. Accordingly, it is plain that requiring Penn-Central to share in the NH's operating losses is merely extending a relationship Penn and Central have already undertaken voluntarily.

In addition, Penn and Central now are in the position to influence the NH's operations through the Approval Committee created under the purchase agreement, and they would have a further voice in this regard if they should participate on the Advisory Committee suggested by the NH trustees. Economies, efficiencies, and improvements effected in current NH operations would benefit Penn-Central when the NH is included in their system.

Furthermore, when we approved the Penn-Central merger, anticipating that Penn-Central would enjoy some $80 million a year in merger savings, we were fully aware that the benefits would be diminished to the extent inclusion of the NH in the Penn-Central system was a negative financial factor. And, in this regard, language in our report in the *NH Train Discontinuance* case, stating that "there is no immediate likelihood of liquidation of the New Haven during 1966 or the next few months thereafter" (327 I.C.C. at 173), indicates that we hoped and expected that Penn-Central would be taking over the NH's operations by this time. On their part, it appears from the record that Penn and Central anticipated, when they reached agreement with the NH trustees on the terms of the purchase agreement, that the NH would be in their system by January 1, 1968.

Penn and Central contend that, if they are required to absorb NH operating losses, the NH creditors would litigate the purchase price endlessly. To support their position they point to language in the reorganization court's ruling of July 11, 1967, where the court advised that this is a contingency which we should guard against. In making this suggestion regarding safeguards, the court assumed that Penn-Central would be bearing the burden of the NH's operating losses. Therefore, the court's admonition does not support Penn-Central's position.[39]

[39] The court's suggestion obviously is sound, and, accordingly, we are making provision to ward off the possibility of undue litigation by the creditor groups as best we can. Similarly, the loan arrangement approved by us makes appropriate provision for maintenance of State aid.

It is our expectation that the findings we have made herein concerning the value of the NH assets and the reasonableness of the consideration to be paid therefor, together with the findings regarding interim support of the NH, will encourage all the parties to direct their best efforts toward complete inclusion of the NH in Penn-Central promptly.[40] We hope there will be no further delay caused by disputes over relatively minor matters.

Operating loss formula and provisions.–The NH trustees propose that Penn-Central participate in absorbing NH operating deficits through an adjustment of the purchase price in amounts calculated under a formula they have presented. The formula is based on net railway operating income with adjustments as follows:

a. The NH's income from the Grand Central Terminal properties, less expenses and taxes related thereto, would be treated as operating income in the amount equal to NH's participation in such incomes as agreed to by Central.

b. Rent for leased roads and equipment, interest on funded debt not in default, and interest on unfunded debt would be treated as operating expenses.

c. Depreciation would be excluded from operating expenses except in the case of certain equipment purchased subsequent to December 31, 1964, as to which the purchase price is reduced under the purchase agreement.

d. Any reduction in public assistance from current levels would not increase the NH deficit for the purposes of the formula.[41]

Using estimated 1967 data for purposes of example, application of this formula would result in charging Penn-Central with $9.1 million of the forecasted $20 million deficit. This is shown in the table below:

Item	*Amount (millions)*
Estimated net railway operating income (deficit)	($20.0)
Grand Central Terminal income	5.0
	(15.0)

[40] The State of Connecticut suggests on brief "that the simplest, most practical and most effective solution to the critical problem of preserving essential New Haven services can be accomplished by an agreement among the creditors, Penn-Central and New Haven, whereby it would be stipulated that upon consummation of the Penn-Central merger, no party would object to having the merged company take title to New Haven property at a price approved by the Commission."

[41] In their brief, the NH trustees have amended the proposed section 9.2.8(d)(ii) of the purchase agreement to refer to the "net" cost of operating certain passenger service unless a contract with the MBTA is in effect.

Item		Amount (millions)
Rent for leased roads	$0.8	
Interest	1.8	
		($2.6)
Depreciation		(17.6)
		8.5
Loss to be absorbed by Penn-Central		(9.1)

We are satisfied that the formula proposed by the NH trustees would be fair, if modified somewhat. Rental for leased roads and interest are more nearly capital charges, that is, costs of providing the railroad plant, and we will not take these items into account. In addition, we do not consider it appropriate to include retirement losses as an item in the formula. While losses on retirement of property are reported as an operating cost, the amount of the loss reflects bookkeeping and other factors involving past years. We do not think that Penn-Central should have to absorb such an item in the circumstances shown here. Adjusting the $9.1-million figure produced above under the NH trustees' proposal for these items ($2.6 million for rent and interest and $1.1 million for retirement losses) reduces the amount of the loss under the formula to $5.4 million.

The next question is how much of this loss should be underwritten by Penn-Central. Two factors carry heavy weight in this regard. One is the admonition of the reorganization court that safeguards should be imposed against the creditors litigating endlessly. The second is that during the period before conveyance of the NH assets to Penn-Central, whether a lease or loan arrangement prevail, the opportunities for integrating the NH's operations into Penn-Central are restricted and, therefore, many operating economies and efficiencies cannot be realized until complete inclusion of the NH takes place. These factors tend to limit the extent to which Penn-Central should be required to assume NH's operating losses during the interim period. In all the circumstances, we shall provide that Penn-Central shall absorb 100 percent of the loss under the formula in the first year, 50 percent in the second year, and 25 percent in the third year.

In addition, we think it unfair to leave open the upper limit of Penn-Central's share of the NH operating loss. While the NH trustees could not predict the amount of the NH's operating losses in 1968 and future years, they indicated that they did not expect future cash attrition to be as large as in 1967. In view of this, it is not likely that the formula would produce a figure as

high as $5.4 million in succeeding years. Accordingly, we shall set a limit of $5.5 million as the maximum Penn-Central share in any year.

The original proposal of the NH trustees required that payment of the trustees' certificates and of the operating losses to be assumed by Penn-Central would be effected through adjustment of the purchase price. Penn-Central seeks the option to apply the trustees' certificates against the purchase price or to hold them for payment by the Estate or for other disposition. On brief, the NH trustees accept the option proposed by Penn-Central.

We are satisfied that a fair balancing of the interests of the various parties can be achieved by adopting a combination of the original proposal of the NH trustees and the treatment sought by Penn-Central. Thus, we shall provide that, pursuant to the price adjustment provisions of the purchase agreement, the trustees' certificates shall be offset in an amount equal to the operating loss to be absorbed by Penn-Central. For example, if the NH trustees had issued $15 million in certificates to Penn-Central, and the operation of the formula we have adopted would require Penn-Central to absorb $10 million in NH operating losses, then the latter certificates would be cancelled, leaving $5 million outstanding. We will grant Penn-Central the election of either retaining these certificates for payment later by the reorganized company; or for other disposition; or for applying toward the price of acquiring the NH assets. The cancellation of the $10 million in trustees' certificates will fulfill Penn-Central's obligation to absorb NH's operating losses. If there were $10 million in trustees' certificates issued to Penn-Central and the latter had to absorb $15 million in NH operating losses under the formula, all the trustees' certificates would be cancelled and the net result would be an increase in the purchase price of $5 million. This treatment should have much the same effect as if operations had been conducted pursuant to a lease.

When all factors are taken into account, the burdens on the NH creditors under the loan program are relatively small, and we are confident not markedly different from what they would be under a lease. As regards the trustees' certificates, we do not believe that the creditors will experience the detriment to their interest in the NH estate that they fear, for it appears that the amount to be issued should be substantially less than $25 million. It is true as the requirements for loan takedowns rise in relation to the operating losses to be absorbed by Penn-Central, the

adverse effect on the creditors increases. On the other hand, as operating losses climb, the burden on Penn-Central increases. For example, as indicated before, based on data estimated for 1967. the net railway operating deficit of the NH, less Grand Central Terminal income, is $15 million. Penn-Central would bear $5.4 million of that total; the remaining $9.6 million would be carried by the creditors. But the entire latter amount is comprised of noncash losses, $8.5 million in depreciation and $1.1 million in retirement losses, which actually have no deleterious impact on the interests of the creditors in the NH assets. It is appropriate to place an obligation on Penn-Central with respect to operating losses because of the influence they can have on operating economies and efficiencies. However, since the amount of the losses to be absorbed by Penn-Central in subsequent years would decrease, there is much to be gained by the creditors in a speedy completion of these proceedings.

The NH trustees ask that, as a closing adjustment, Penn-Central pay cash for its share of operating losses. This deviates from the purchase agreement which now gives Penn-Central the option of paying for purchase price adjustments in bonds, stock, or cash. The NH trustees seek this relief on the ground that they need cash to implement their plan of reorganization. However, we are not persuaded that this is a sufficient reason to place the burden of paying in cash on Penn-Central, and we shall leave the existing provisions of the agreement undisturbed in this regard.

Traffic protective conditions.– Reading and CNJ request that the traffic protective conditions they proposed at the NH inclusion hearing be made effective with the commencement of whatever arrangement we may approve. Moreover, Reading insists that Penn-Central assistance to the NH during the interval between consummation of the Penn-Central merger and inclusion of the NH in that system buttresses the need to begin the protection period with the date of the Penn-Central union.

EL asks that, pending its inclusion in a major railway system, the revised conditions of appendix G be made applicable to any interim arrangement under which Penn-Central assume control of the NH traffic. In addition, if any arrangement for control of the NH's operations by Penn-Central be imposed, EL avers that we should adopt the permanent protective conditions it submitted in the NH inclusion hearing.

We have determined that certain conditions should be imposed to protect WM, Reading, and CNJ. See *infra*, sheets 123 *et seq.*

Those conditions will take effect on the date of consummation of the Penn-Central merger and their acceptance in writing by WM, Reading, and CNJ. To the extent Reading and CNJ seek any additional traffic protection, for reasons given hereinafter their request is denied.

Our decision with respect to interim support for the NH does not grant Penn-Central control of the NH's traffic. Therefore, we need not deal with EL's request.

FINDINGS UNDER SECTION 77 OF THE BANKRUPTCY ACT.

At this juncture, further consideration of section 77 of the Bankruptcy Act, 11 U.S.C. 205, is required. One of the issues in these proceedings is whether we are authorized to make findings with respect to equitable terms for inclusion of NH under section 5(2)(d) prior to our consideration and approval of a complete plan of reorganization under section 77. Interrelated with this issue is whether we are empowered or required to make any findings under section 77 in advance of our consideration of a complete plan of reorganization, and, if so, what findings are necessary and appropriate. Several creditors contend that the terms of the sale as well as of the distribution should be submitted to a vote of the creditors.

At the outset, it is to be noted that the bankruptcy procedures of section 77 are available to any railroad that is insolvent or unable to meet its debts as they mature and desires to effect a plan of reorganization. NH has availed itself of these procedures. As an emergency measure, section 77 has as a primary purpose the preservation of the rail transportation network and thus promotion of the public interest. At the same time, section 77 requires that private interests be protected and balanced with the public interest in continuation of rail service.

Section 77(b) sets forth what a plan of reorganization *must* include, and what it *may* include. The first clause of section 77(b) provides that a plan "shall include provisions modifying or altering the rights of creditors generally, or of any class of them, secured or unsecured, either through the issuance of new securities of any character *or otherwise* * * *" (emphasis supplied). Although this is a mandatory provision, there is nothing in its language which requires that all facets of a plan of reorganization be carried out at the same time or that the terms of the modification or alteration be considered before the properties may be evaluated or sold.

The second and third clauses, dealing generally with the rights of stockholders and the issuance of new securities, are permissive, while the fourth and fifth caluses are framed in mandatory language. Clause (4) requires adequate coverage of fixed charges for the reorganized railroad, and has little relevancy to the question at hand in the present circumstances. Clause (5) requires that the plan provide adequate means for the execution of the plan, which may embrace the transfer of all or any part of the debtor's property to another corporation, the merger or consolidation of the debtor with another corporation, and other alternative means, including any other appropriate provisions not inconsistent with section 77. Among the permissible alternatives set forth in section 77(b)(5) is the sale of all or any part of the debtor's property either subject to or free from lien at not less than a fair upset price. Many of the provisions following clause (5) are of a permissive nature. Except for clauses (1), (4) and (5), there is no provision in section 77(b) or elsewhere in section 77 which deals specifically with the form or content of a plan of reorganization. Thus, there is no language in section 77 prohibiting our evaluation of the debtor's properties and approval of their sale before approving the restructuring of the debtor. Nor does its legislative history indicate Congressional intent to impose such a prohibition.

Moreover, under chapter X "two-step" plans of reorganization have had judicial sanction in situations in which the debtor's assets were wasting away, either physically or financially. In such cases, the sale of the debtor's assets has been allowed, while matters pertaining to the priority, validity and satisfaction of claims were deferred to a later date. See *In re V. Loewer's Gambrinus Brewery Co., Inc.*, 141 F. 2d 747 (1944). At page 749, the court stated:

> The appellant lays great stress upon the fact that here the sale was of all income-producing property of the debtor and hence was likely to prevent the adoption of any plan of reorganization and to defeat the very purpose of the reorganization proceeding. But the disposition of the property could not be longer delayed without peril to all interests. The properties were wasting assets' **

The doctrine of wasting assets is applied to situations involving either physical or economic loss. *In re The Sire Plan, Inc.*, 332 F. 2d 497 (1964); *In re Pedlow*, 290 Fed. 841 (1913); *In re Rosenbaum Grain Corp.*, 83 F. 2d 391 (1936); *Hill* v. *Douglass*, 79 F. 2d 851 (1935).

While the *Gambrinus* case arose under chapter X, and thus does not control the situation here, its rationale is highly persuasive and should be applicable to NH, which is clearly a "wasting asset." We believe that a court would reach a similar decision in this proceeding in view of the broad equitable powers conferred by section 77 upon reorganization courts. (See section 77(a)). For reasons stated above, we conclude that under the unique circumstances presented here the trustees' two-step concept of reorganization is not inconsistent with section 77.

The legality of this concept was questioned before the United States Court of Appeals (2d Cir.) in docket No. 31082, *In the Matter of the New York, New Haven and Hartford Railroad Company*, 378 F. 2d 635, and the court rules that a decision by it at that time would be premature. Though viewing the plan with certain reservations, the court approved its presentation to this Commission, noting our assigned function in the architecture of railroad reorganization plans. Since the ruling of the court, the NH's situation has seriously deteriorated, placing in imminent jeopardy the continuity of NH service required by the public convenience and necessity. The press of time has become materially more significant. We do not view the court's ruling as precluding our consideration and approval of a two-phase plan, but rather as an admonition to proceed with the greatest deference toward all the interests involved in this complex, critical and sensitive area of regulation.

The first part of the trustees' plan provides that creditors' interests will shift from a lien on the present assets of NH to a lien on the assets which the trustees will hold following the sale to Penn-Central. Provision is made for the preservation of priority and rights of claimants after sale of the assets. As an integral part of the second step, provision will be made for the modification or alteration of creditors' rights, the treatment of the rights of all claimants, and the ultimate distribution of the assets of the estate or securities of NH, subject to approval by this Commission and the reorganization court. Under the circumstances, we believe the rights of creditors and claimants are fully protected. The fact that the sale will be free from lien does not improperly alter the rights of creditors because the proposal before us specifically provides that their present liens or claims are to be transferred to the proceeds of the sale. *Van Huffel* v. *Harkelrode*, 284 U.S. 225 (1931); *Gardner* v. *New Jersey*, 329 U.S. 565 (1947). Nor does the omission of a vote on the proposed sale or

on the consideration thereof violate the rights of creditors. *In re V. Loewer's Gambrinus Brewery Corp., supra; In re The Sire Plan, Inc., supra; In re Rosenbaum Grain Corp., supra; Hill* v. *Douglass, supra.* Because of the two-step concept of the plan, which is highly essential and in the public interest in these proceedings, no vote need be taken with respect to the first step of the plan.

While it may be unusual to determine the value of NH in advance of and separate from a complete plan of reorganization, such procedure is not prohibited by the terms of section 77, and it appears to be within our discretion to make such a finding. *In Re Plankington Bldg. Co.*, 40 F. Supp. 517 (1941). Under section 77 we are the chief architect of any plan of reorganization. *St. Joe Paper Co.* v. *Atlantic Coast Line R.R.*, 347 U.S. at 32[illegible]. The valuation must be made in accordance with the standards set forth in section 77(e),[42] and is a matter essentially within the province of this Commission. *Ecker* v. *Western Pacific R. Corp., supra.* Since valuation for reorganization purposes is made up of many imponderable factors which cannot be reduced to a fixed formula, precise findings as to value are not necessary. See *Group of Investors* v. *Milwaukee R. Co., supra.* Although earning capacity is usually looked upon as the principal criterion in valuing railroad properties, due consideration may be accorded to other relevant factors, including original cost of the properties, cost of reproduction new, cost of reproduction depreciated, actual investment therein, severance or strategic value, contributed traffic, value of particular facilities, and the effect of potential operating economies. We have given due consideration to past, present and prospective earning power as well as to other relevant factors specified in section 77(e), including reproduction and original costs, and, additionally we have considered the liquidation value of NH—finding that value to be $125 million, a figure comparable to the price in the purchase agreement. Moreover, the liquidation value of the NH properties in the context of the NH's present situation exceeds the fair upset

[42] Section 77(e) provides in part:

> The value of any property used in railroad operation shall be determined on a basis which will give due consideration to the earning power of the property, past, present, and prospective, and all other relevant facts. In determining such value only such effect shall be given to the present cost of reproduction new and less depreciation and original cost of the property, and the actual investment therein, as may be required under the law of the land, in light of its earning power and all other relevant facts.

price, and as indicated, under section 77(b)(5) all or any part of a debtor's property may be sold at not less than a fair upset price.

Those who have a valuable interest in the NH estate could not, under circumstances favorable to them in a liquidation, expect to effect a greater net return than would be accorded them under the plan we are approving herein for the sale of the assets to Penn-Central. All have had fair and ample opportunity to present evidence and argument on the question of valuation, and we find the record entirely adequate to make possible and to support findings as to that issue for all purposes of section 77 of the Bankruptcy Act as well as section 5(2) of the Interstate Commerce Act. Accordingly, the sale of NH assets to Penn-Central under the terms of our decision herein is consistent with section 77(b)(5) in that it provides an adequate means by which the trustees' plan can be executed. We also find that the consideration to be paid for the assets of NH constitutes just and adequate compensation. As we view the situation, the parties holding a present interest in NH will receive the economic equivalent of what is surrendered upon the sale of the NH assets. We further find under section 77(e) that this valuation and those aspects of the trustees' plan dealing with sale of the considered NH assets is fair and equitable; and that the interests of security holders, creditors, claimants, and other persons involved will not be adversely and materially affected. We further find under section 77 that the trustees' plan to the extent approved herein is compatible with the public interest.

Our remarks and findings here with respect to section 77 are not to be construed as prejudging the remaining portion of NH plan of reorganization. The terms of distribution of the assets following the sale and the ultimate modification or alteration of the rights of creditors will be the subject of further proceeding.

MOTOR CARRIER RIGHTS

The New England Transportation Company (NET), a NH motor carrier subsidiary, engages in both motor-rail coordinated services and in independent motor common carrier operations through rights originating under the "grandfather" provisions of the act. It is predominantly a general commodity carrier operating over regular routes in Rhode Island, New Jersey, New York, Massachusetts, and Connecticut. As of December 31, 1965, it owned 255 pieces of equipment, consisting of 21 trucks, 116 tractors, and 118 trailers. In 1965 its gross operating revenues totaled

$3,318,690, approximately 60 percent of which were derived from independent common carrier movements. However, it suffered a net deficit of $108,734, and has consistently operated at a loss.

Supporting testimony of shippers utilizing NET's service indicates NET furnishes a highly personalized service, tailored to the requirements of its shippers, some of whom have been customers for almost 3 decades. These shippers have partially built up their businesses relying upon NET's service and to abrogate NET's operation at this time could jeopardize their competitive position.

NET's operating area is served by other motor common carriers, none of which has intervened in this proceeding. The record does not show the extent of these carriers' operations or of the actual competition existing between them and NET.

It is evident that NET's operations fulfull an important public need for motor carrier service. The continuation of that service is in serious jeopardy because of the NH's dire financial condition. However, the transfer of the operating rights of NET to the control of Penn-Central should assure that the service will be preserved.

Under the principle of the *White Line* case, *Rock Island M. Transit Co.–Purchase–White Line M. Frt.*, 40 M.C.C. 457 (1946) and 55 M.C.C. 567 (1949), motor carrier operating rights of a railroad or its affiliate should usually be restricted solely to a service "auxiliary to and supplemental of" train service of the railroad. For reasons set forth below, application of that principle here is not warranted.

NET is presently an affiliate of a railroad and yet its operating rights are generally not limited to a service "auxiliary to and supplemental of" train service. There is no evidence that any motor carrier has been adversely affected by NET's operations. In these circumstances, convincing reasons would have to be advanced to justify imposing restrictions. This record contains none.

While it is true that Penn-Central would be a strong company with substantial financial resources at its disposal and that it, therefore, presumably could develop NET into a more formidable competitor than NET has been under the control of the NH, there is nothing in this record which even hints that control of NET by Penn-Central would result in an undue restraint of competition. In this connection it should be noted that the primary objective of the principle of the *White Line* case is to protect motor carriers from the dual competition of an all-motor service in addition to

rail service. See *American Trucking Assn. v. U.S.*, 364 U.S. 1 (1959). It is most significant, accordingly, that no motor carrier has appeared in the instant proceedings. *Burlington Truck Lines, Inc.–Purchase–Pirnie*, 85 M.C.C. 363, 372–373 (1960).

Furthermore, the unrestricted operating rights of NET make a vital contribution to the carrier's overall operations, and if NET were compelled to rely solely upon rail-related traffic its losses would increase, thereby inducing Penn-Central to curtail or seek abandonment of substantial portions of the operations. This would have the additional effect of further weakening the operations of the NH, for an all-rail service would be even more unprofitable and inefficient. Such developments would not be consistent with the public interest, and clearly this Commission would be remiss in carrying out its responsibilities if its actions were to stimulate such consequences.

The operations of both Penn's and Central's motor carrier affiliates are primarily restricted to service which is incidental and auxiliary to the parent lines' rail operations in contrast to the nonrestricted motor carrier service of NET. In respect to the points served there is only a limited overlap in operating authorities, i.e., Worcester, Boston, Springfield, and possibly a few other Massachusetts points, and also points and stations in the metropolitan New York area, particularly those in Westchester County, New York. The duplication in operating rights will be minimal and no undue restraint of competition should result from the change in control. However, the duplications should be eliminated to the extent they exist. Therefore, similarly to our order of April 6, 1966, 327 I.C.C. at 551, treating with duplications in the operating rights of motor carrier affiliates of Penn and Central, we shall require Penn-Central, within 2 years from the date of the inclusion of the NH, to submit a plan for the elimination of such duplications or inconsistencies as may exist among the authorities held by the motor carrier affiliates, including NET, controlled by Penn-Central. Jurisdiction is reserved to this Commission to require consolidation of any or all of such motor carriers on its own motion if such action is deemed to be in the public interest.

We, therefore, find that acquisition of NET is consistent with the public interest and that Penn-Central can use the motor vehicle service to public advantage in its operations. Furthermore, the record shows that future operations of the motor-carrier service will not restrain competition, and that there is a compelling public interest not to impose the auxiliary or supplemental

restrictions. Jurisdiction will be retained, however, to prescribe whatever restrictions or conditions, if any, appear necessary in the public interest in order to adhere to National Transportation Policy. See *Burlington Truck Lines, supra*, 85 M.C.C. at 374.

EMPLOYEE PROTECTIVE CONDITIONS

On May 20, 1964, Penn and Central and 23 unions, representing approximately 75 percent of the above-named carriers' total labor force, entered into a labor protective contract entitled "Agreement for Protection of Employees in Event of Merger of Pennsylvania and New York Central Railroads." The substance of this agreement is described in the initial report in these proceedings, 327 I.C.C. 475 at page 543, *et seq.*, and need not be restated.

Section 2 of the agreement provides for the future coverage of employees of other carriers whose inclusion in the primary merger we may require. Pursuant to this section, both Penn and Central executed agreements with labor organizations representing approximately 98 percent of NH's union force.[43] These agreements apply the provisions of the May 20, 1964, contract to NH employees with certain exceptions and qualifications.

The basic merger protective agreement is supplemented by alternatives and benefits available to those employees subject to transfer outside a 35-mile radius of their present location. The signatory unions will enter into implementing agreements with Penn-Central providing for the transfer and use of employees and reallocation of forces made necessary by the changes resulting from the inclusion.

On December 3, 1966, NH had 10,294 employees in active service. Penn-Central estimates that 1,257 positions will be abolished as a result of NH's inclusion. However, 51 local and 515 distant jobs are expected to be created, thereby reducing the number of jobs lost to 691. Multiplying this number by the average annual salary, the net annual reduction in payroll is estimated by Penn-Central at more than $5,300,000.

The first 5 years of Penn-Central's costs for protecting NH's employees will total $13.5 million, leaving the balance of the $14.1

[43] Agreements were executed on December 20, 1966, with the Brotherhood of Locomotive Engineers, January 9, 1967, with the Brotherhood of Locomotive Firemen and Enginemen, and January 19, 1967, with 17 international and national labor organizations.

million cost, previously discussed, to be paid over a subsequent period of years.

The creditor groups estimate the average annual cost to be $8.0 million. The variance in the two estimates is primarily caused by the creditor groups' contentions that furloughed employees are not qualified "present employees" under the agreement and, therefore, may not receive any protective benefits; and that changes in respect to both function and manpower will not take place simultaneously with the merger, and, therefore, the costs of labor protection for all of the surplus employees will not begin on the date of the merger. We are satisfied that the Penn-Central estimate of labor costs is better grounded than the estimate of the creditor groups.

Penn-Central indicates that the agreements signed with the NH employee representatives are of the type contemplated by section 5(2)(f) of the Interstate Commerce Act and make it unnecessary for us to prescribe conditions for the protection of these employees. Penn-Central offers to provide the same protection to nonsignatory employees.[44]

We find that the agreements signed by Penn and Central with NH employee representatives do not render the inclusion inconsistent with the public interest. We will not make any requirement for the protection of employees covered by these agreements. As to affected employees not represented by the signatory unions, for reasons set forth in our earlier report, 327 I.C.C. at pages 544–546, the agreements between Penn and Central and the signatory unions afford fair and equitable employee protective conditions pursuant to section 5(2)(f). Furthermore, as provided in that report, we shall require the nonsignatory employees to enter a commitment in writing to Penn-Central indicating their agreement to the plan. If, within 30 days after the time an employee is first notified by Penn-Central that he will be affected in his employment as a result of the inclusion, the employee fails to indicate his intention in regard to the protective benefits, he will be presumed to have chosen recourse to other benefits. On the other hand, Penn-Central shall inform the nonsignatory employees of the terms of the basic agreement of May 20, 1964, and the manner in which said terms shall be extended to NH employees. This

[44] In addition, Penn-Central is willing to extend to officers of NH who may be adversely affected by NH's inclusion in Penn-Central the same privileges and benefits that will be granted officers of Penn and Central adversely affected by the Penn-Central merger.

notification shall be accomplished prior to or at the same time the employee is first informed that his employment will be affected.

TRAFFIC CONDITIONS

As a result of NH's inclusion in Penn-Central, some form of protection against diversion of traffic, including indemnification, is sought by CNJ, Reading, WM, B&M, D&H, and EL. In addition, the NH creditor groups request that NH be sheltered from diversion of traffic resulting from the Penn-Central merger until NH is included. Although initially the NH trustees did not believe the NH required any such safeguard, at oral argument they modified their position to ask jurisdiction be reserved over this matter so that at a subsequent time we can consider the impact of the Penn-Central merger upon NH's traffic and, if warranted, make appropriate adjustments in the consideration to be paid by Penn-Central for NH assets.

CNJ, READING, AND WM

CNJ, Reading, and WM seek the same protection, and we shall treat their contentions first. CNJ and Reading are primarily short haul, overhead carriers largely dependent upon interline business. WM, although in some respects a trunkline, long-haul railroad, in connection with traffic interlined with NH acts as a bridge carrier. The above-named lines shall be hereinafter collectively referred to as intervenors. Their corporate structures, routes and operations have been discussed in detail in our prior reports in these proceedings.

In assessing the impact upon them of NH's inclusion in Penn-Central, CNJ, and Reading insist that we must consider evidence of the adverse effect of the Penn-Central merger itself. They assert error in the exclusion of such evidence from the record by the hearing examiner. This problem of the untimely submission of evidence concerned with the Penn-Central merger has now been raised several times at different stages of these proceedings. For reasons set forth in prior reports, see particularly 328 I.C.C. at pages 316-318 and 330 I.C.C. at pages 356-357, we affirm the examiner's ruling.

The intervening parties claim inclusion of the NH in Penn-Central will divert substantial amounts of traffic from their respective lines, eventually impairing their ability to maintain their present services. They argue that the diversion will arise for two

reasons, the first being the increased service advantage the merged system will have stemming from its ability to provide direct single-line north-south and east-west service and more specialized equipment. The second reason alleged by intervenors is the anticipated downgrading of gateways through which they presently interchange traffic with NH. Thus, they claim that Penn-Central's utilization of the Selkirk, N.Y., gateway for east-west traffic to and from NH territory will result in downgrading the Maybrook gateway to a point where service through that gateway would not be competitive with the service via the Selkirk facility. Intervenors contend that Penn-Central's equivocal attitude toward rehabilitation of the NH bridge across the Hudson River at Poughkeepsie, N.Y., which is vital to the operation of the Maybrook gateway, corroborates their suspicions. Furthermore, they question the merged company's intent in regard to the retention of NH's float service across the New York Harbor, arguing that, because the service is costly, slow, and affected by weather conditions, an alternate route will be found.

Each intervenor stresses the vulnerability of its overhead traffic to diversion. CNJ claims that its overhead traffic is subject to diversion where there are alternate competitive routes of the Penn or Central by which the traffic could move to or from the NH. Based on 1966 data, they contend such traffic amounts to 52,530 carloads, producing revenues of $1,534,666. Approximately one-half of this traffic originated or terminated on lines other than the "family lines." In addition to this traffic, CNJ claims as divertible 2,836 carloads, yielding $329,400 in revenues, either originating or terminating at points on its line which are also served by Penn or Central in conjunction with the NH. The total traffic claimed as subject to diversion, i.e. $1,864,067 in revenues, represents 4.6 percent of CNJ's total freight revenues for 1966.

The overhwelming bulk of Reading's claimed divertible traffic is also overhead.[45] Reading concludes that based upon May 1965 and 1966 study data, which showed revenue subject to diversion to be $102,719 and $137,013, respectively, the projected annual loss would be between $1,214,000 (1965) and $1,539,000 (1966), or 1.3 percent and 1.7 percent of the total freight revenues for those respective years.[46] In arriving at these estimates, Reading excludes from the total volume of overhead traffic a number of

[45] Eighty-five percent of Reading-NH interlined traffic is overhead to Reading, while 19 percent is overhead to NH.

[46] Reading's projected divertible traffic is based upon a study of its own records for May 1965 and a printout of NH data for May 1966.

categories[47] as being nondivertible, the most important and largest being bituminous coal traffic. Reading believes some of its traffic movements either originating or terminating on its lines at points which could be served by the Penn or its subsidiary, the Lehigh Valley Railroad Company, could also be diverted.

WM included within its estimate only bridge traffic for which there were published actual alternate routes via the Central or Penn. No traffic originating or terminating on its line is considered as divertible. Based upon May 1966 data, WM contends that 37,524 cars producing $962,196 in revenues would be diverted. This represents approximately 2 percent of WM's gross revenues for 1966.

Intervenors join in seeking imposition of the conditions propounded by Reading. These provisions would extend most of the protective devices established in appendix G to our initial report, 327 I.C.C. at page 561, together with the indemnification provision as first granted therein and as later amended in our supplementary report, 330 I.C.C. 328. The protective period for these "temporary" conditions would commence upon consummation of the Penn-Central merger and would terminate with the inclusion of each of the intervenors in either the N&W system or another major system. At that time the "permanent" protective conditions would attach. These are designed to maintain the relationships and competitive status which prevailed among intervenors and Penn-Central, and NH prior to the Penn-Central merger and NH's inclusion therein. The conditions are in part similar to the standard traffic conditions (appendix I, 327 I.C.C. at page 564) and additional conditions (appendix H, 327 I.C.C. at page 563) imposed in our initial report and those proposed herein by Penn-Central. These conditions would be terminated upon the agreement of the parties then representing intervenors with Penn-Central or upon our order.

Penn-Central oppose the imposition of any protective conditions, claiming that inclusion of the NH would have no significant adverse effect on intervenors' traffic. In support of their position, Penn-Central state that they intend to retain the Maybrook and Jersey City gateways and that these facilities will not be downgraded. Moreover, they maintain that a survey conducted by Penn personnel, who interviewed the persons controlling the routing of the

[47] Interterritorial and intraterritorial traffic for which there are generally no established Penn or Central routes or station facilities.

multiple-car shipments listed on the NH May 1966 print-out,[48] establishes that routing practices would not be affected by the NH inclusion.[49]

Penn-Central submit proposed conditions in the event we should find them necessary. These proposals, like Reading's, are modeled on appendix H to our April 6, 1966 report, 327 I.C.C. at page 563, and require the maintenance of all existing or comparable routes via existing or comparable gateways, neutrality in handling NH originated or destined traffic in order to permit equal opportunity for service to and from intervenors' lines, and mutual cooperation between these parties in order to continue and improve the NH-CNJ-Reading-WM route as a competitive route between points located on or beyond NH's lines and points located on or beyond the lines of the intervening parties. Neither side would be able to change the schedules or take any other action which would increase the transit time via the aforementioned route or adversely affect the standards of service without the written consent of the other. Although Penn sought release from the obligation of maintaining a noncompensatory NH float service, it is agreeable to a condition requiring continuance of this service indefinitely or with agreed changes subject to the approval of the intervening lines.

Penn-Central's proposals do not contain indemnity provisions. It is their position that the amount of indemnification would be inconsequential and this type of provision would assume the nature of an insurance policy protecting against loss of traffic from wholly unrelated causes. Penn-Central is also agreeable to the institution of these conditions upon the date of consummation of the Penn-Central merger.

Collectively more than 80 percent of traffic interchanged by intervenors with the NH is overhead. The fact that this type of traffic is most vulnerable to diversion is well known. However,

[48] See footnote 50.

[49] CNJ urges that the hearing examiner erred when he received in evidence appendix 1 to NHI-120 over intervenor's objections based on its hearsay nature. This appendix contains an analysis reflecting the Penn-Central survey.

We affirm the examiner's ruling. The fact that evidence may be hearsay does not necessarily mean an administrative agency must reject it. The sponsoring witness was fully competent to testify on the subject matter. Intervenors were informed of, or could have ascertained, all pertinent information concerning the survey, including the identities of the persons contacted, the questions asked and representations made by Penn personnel, and the answers given. No claim is made that the intervenors were hampered in their cross-examination of the Penn-Central witness by the hearsay element. In short, intervenors have failed to demonstrate that they were prejudiced by the examiner's ruling.

because approximately half of CNJ's claimed divertible traffic, 5/8 of Reading's overhead traffic, and possibly an even greater proportion of WM's overhead traffic interchanged with NH either originates on or is destined to points on the B&O or C&O, we do not have a typical overhead situation. The identity of interest between the various members of the B&O-C&O family has been discussed in our prior reports herein and in the *N&W Inclusion* case, and certainly the wide scope of C&O-B&O operations and solicitation resources are bent to intervenors' welfare. The record clearly shows that the services provided by the B&O to the various coal shippers is of superior quality and fully competitive. Because of the quality of this long enduring, efficient and personal service it appears that certain industrial and mining patrons would divert traffic away from the intervenors only if the Penn-Central should provide a vastly superior service.

On the other hand, Penn-Central's traffic survey is premised on the theory that inclusion of the NH in the Penn-Central system would not result in improved service. This premise cannot be accepted. It is clear that shippers obtain service advantages from single-line service and more flexible car supply. See 327 I.C.C. at pages 490-491. Moreover, Penn-Central proposes improvements, particularly those related to operations through Central's Selkirk yard, which will provide better service and a more economical operation to all points on NH. Therefore, it is reasonable to conclude that inclusion of NH in Penn-Central will have an adverse impact on intervenors' traffic.

Balancing these considerations, it appears to us that diversion of approximately $828,828,[50] $845,057,[51] and $481,098,[52] in annual revenues from CNJ, Reading, and WM, respectively, may reasonably be expected from NH's inclusion in the Penn-Central system. WM is a strong carrier, to be directly controlled by a major eastern system. It can absorb such losses. The financial problems of CNJ and Reading are more deep-rooted but we cannot ignore the fact that they also are part of the C&O-B&O family. Requiring Penn-Central to protect these carriers against circumstances which, except to a minor extent, are not caused by Penn-Central does not appear fair.

[50] Overhead traffic neither originating nor terminating on family lines.

[51] Overhead traffic foreign to family lines plus divertible forwarded or terminated traffic, excluding bituminous coal.

[52] Overhead traffic estimated to be neither originated nor terminated on family lines.

We are persuaded that the crucial consideration raised by the evidence in relation to the intervenors' operations does not concern the direct diversion they may suffer from inclusion of NH in the Penn-Central system but the diversion that would result if the Jersey City and Maybrook gateways were downgraded. The competing routes to New England participated in by intervenors and Penn both use the Jersey City and Maybrook gateways as a passage to NH territory. Penn intends to continue using the Jersey City gateway for traffic moving into and through the metropolitan New York area and points in southern New England served by NH, although some traffic will move via Selkirk after inclusion. It is possible, as Penn-Central maintains, that service via the harbor may improve with a reduction of traffic because of less congestion and less handling of cars. However, service at this point will remain dependent upon weather conditions, the availability of floating equipment, the maintaining of coordinated rail-water interchange schedules, and various other factors.

The immediate elimination of the New York Harbor service seems improbable. The alternate proposal utilizing the New York, Susquehanna & Western Railroad Company along the central west shore route through Selkirk, there connecting with the Boston and Albany Division (B&A) of the Central for ultimate interchange with the NH, is not feasible because of the great circuity of the route and the lack of adequate interchange facilities for the added volume of traffic. The completion of improvements to the Selkirk facility or the construction of another facility in the vicinity of the New York metropolitan area on the west bank of the Hudson may well change the situation, but this possibility does not now offer a threat to intervenors' traffic.

Penn-Central intends to use the Selkirk gateway for traffic moving between points west of Columbus, Ohio, on the one hand, and New England on the other. Traffic emanating east of Columbus, Ohio, will still be routed via Maybrook. Traffic using the Selkirk gateway will be interchanged with the B&A and then interlined with the NH. The use of B&A improves the service and provides a more economical operation at the Framingham, Worcester, and Springfield, Mass., junctions. The modern Selkirk facility will permit the achievement of numerous efficiencies and economies. See 327 I.C.C. at page 490. Use of this gateway will enable eastbound freight trains to be classified for direct dispatch to terminals or consignees in New England without the necessity for further handling or interchange.

Approximately one-third of CNJ's, two-thirds of Reading's, and perhaps an even larger percentage of WM's NH interchanged traffic traverses the Maybrook gateway. Both the Alphabet and Central States Despatch Routes in which intervenors participate use the Maybrook gateway as an entrance to the northeast. The Alphabet Route in particular is considered a vital freight route between midwest and western points, on the one hand, and New England points, on the other. It provides competition to the long-haul routes of the B&O, Central and Penn within this territory.[53] See *Chesapeake & O.–Control–Western Maryland, supra*, 328 I.C.C. at page 700. To cut down in services at the Maybrook gateway would hamper the efficiency of both the above-mentioned routes, gradually causing their demise as competitive routes to the Northeast.

In these circumstances, C&O-B&O, third and smallest of the major eastern carriers, assuming consummation of the Penn-Central merger and inclusion of EL, D&H, and B&M in the N&W system, would be left without an equivalent access route into New England. Penn-Central would have Selkirk and B&A, N&W would have Mechanicsville, N. Y., and B&M. In the face of such competition and without a competitive gateway into New England, the ultimate impact on the intervenors could be serious and detrimental to the shipping public, which would lose an effective choice of the C&O-B&O family lines service to and from the NH territory. If intervenors were to be included in the N&W system as is contemplated in the application in the N&W-C&O case,[54] the need for this third gateway to New England may end. Therefore, we shall impose protective conditions pending decision in that case.

Our objective can be accomplished by imposing conditions suggested by Penn-Central. These conditions differ from those offered by the Reading in respect to indemnification, mode of enforcement, and period of inception. Otherwise, the basic protective conditions vary only in the manner of expression. We adopt Reading's suggestion that the conditions become effective as of the date of the consummation of the Penn-Central merger and also certain of the language it has proposed which we believe more effectively achieves our objective. However, we have incorporated the language set forth in appendix G in *Chesapeake & O. Ry. Co.–Control–Western Maryland Ry. Co.*, 328 I.C.C. 684 at page 761, into the enforcement provision. The prohibition against

[53] It simulates in some respects a single-line service, for trains are handled in an expedited manner with through crews, power, and cabooses.

[54] Finance Docket No. 23832.

shifting of traffic to the Selkirk gateway is adequately covered within the terminology of these conditions. We believe the imposition of these conditions, which are set forth in detail in appendix I, will maintain Maybrook and the New York Harbor as vital and competitive passages to New England and as a result the diversionary effects of the NH's inclusion in Penn-Central will not be serious. We believe imposition of indemnification provisions are not warranted, and, except to the extent indicated, we deny the requests of CNJ, Reading, and WM for indemnification and other relief.[55] Jurisdiction will be retained in order to consider the extent to which modifications in a changing situation may be necessary to protect the public interest.

D&H, B&M AND EL.

It is the position of D&H that the Penn-Central merger should not be consummated prior to D&H's inclusion in one of the major Eastern systems and that, even if the Penn-Central merger should be consummated before such inclusion, NH's inclusion in Penn-Central should not be permitted until the inclusion of D&H in a major system. If this position should not be accepted, D&H requests imposition of the conditions it sought in the proceedings concerning appendix G of our initial report.

B&M states that its needs for protection are met by the standard protective conditions and the proposal it made in the appendix G proceeding.

Subsequent to close of the hearing in the instant proceeding, we issued our supplemental report and order on reconsideration and further hearing in the appendix G proceeding, 330 I.C.C. 328. Among other things, we provided for inclusion of NH in the definition of "merged company." 330 I.C.C. at pages 336–337. Neither D&H nor B&M has sought reconsideration of that report. Accordingly, it appears that the requests of D&H and B&M for protective relief have already been appropriately handled. In view of the protection granted D&H, its requests for deferral of the Penn-Central merger and NH's inclusion in Penn-Central are denied. No further action is required here.

EL also requests extension of the appendix G conditions to the NH operation pending its inclusion in a major system in addition to the standard routing conditions referred to above. Further-

[55]The standard traffic conditions imposed in our initial report, 327 I.C.C. at page 564, will continue to remain in effect after NH's inclusion.

more, EL seeks permanent protective conditions, effective from the date of our order authorizing NH's inclusion in Penn-Central and continuing in effect after EL's inclusion in N&W. These conditions are explicitly geared to require Penn-Central to maintain the competitive status of the Maybrook gateway. Generally, the terms of the proposed conditions also require all present operating routes, gateways, rate divisions, solicitation policies, and routing practices to be maintained.

Penn-Central contends that EL's proposal in regard to the enactment of permanent conditions is not consonant with our intention, for by seeking imposition of permanent conditions, EL is really seeking a built-in competitive advantage for itself and the N&W system.

Our expressed purpose in imposing appendix G protective traffic conditions is to guard against the adverse effects of the Penn-Central merger in order that the adversely affected carriers may be able to maintain their necessary operations until their future is determined. 327 I.C.C. at pages 531-532. EL's proposal would have us go much farther. By imposing conditions of the type suggested, we would not be merely sustaining a necessary operation until it could fend for itself, but we might well be creating a permanent division of markets with undesirable effects on the competition.

It should be noted that N&W has not requested the imposition of any conditions in this proceeding. Evidently, through prescription of the conditions it has proposed, EL hopes to gain some protection against N&W adopting a policy of employing the Mechanicsville gateway to and from New England and thereby short-hauling EL. Penn-Central should not have to shoulder the responsibility of safeguarding EL from its parent. In any event, so long as the conditions imposed to protect CNJ, Reading, and WM remain in effect, they would also benefit EL.

For the aforementioned reasons, we deny EL's request for permanent conditions. Insofar as temporary protective conditions are concerned, our decision in 330 I.C.C. 328 eliminates any need for action herein.

NH

In addition to the standard traffic protective conditions, the NH creditor groups ask that the NH be indemnified for any loss of traffic caused by the Penn-Central merger.

The standard traffic protective conditions imposed in the report of April 6, 1966, will apply insofar as NH is concerned until its inclusion in Penn-Central. The record does not justify the imposition of indemnification provisions.

We said in our report of June 9, 1967, 330 I.C.C. at page 333:

> The protective conditions as originally prescribed in appendix G are directed towards the establishment and maintenance of temporary restraints upon the merger transaction to the extent necessary to preserve the integrity of the protected railroads and prevent a significant curtailment in the amount and quality of services which those carriers now provide for the shipping public.

The evidence here indicates that the Penn-Central merger will not have any significant adverse effect on the NH for several years. Before any such effect occurs, the NH should be included in Penn-Central. Moreover, we have provided herein interim support for NH by Penn-Central pending consummation of the inclusion. It is not unreasonable to believe that the transfer of the NH assets to Penn-Central ownership will have passed before the NH suffers any important loss of traffic. If any unusual or unforeseen circumstances warrant our reconsideration of this matter, our general reservation or jurisdiction in this case can serve as a means for reexamining our position and further examining price. See *Oscar Gruss & Son* v. *United States*, 261 F. Supp. 386, 390 (S.D. N.Y. 1966), affirmed 386 U.S. 776.

SECTION 20A PROCEEDING

In Finance Docket No. 24361, Penn seeks authority under the provisions of section 20a(1) to issue 950,000 shares of its common stock, par value $10 per share, or such number of shares as results from the price adjustments and antidilution provisions of the purchase agreement; (2) to issue $23-million principal amount of 25-year divisional first mortgage bonds, or such adjusted amount as it produced by operation of the adjustment provision of the purchase agreement; and (3) to assume obligation and liability in respect of (a) equipment trust obligations guaranteed by NH, (b) bonds and certificates of contingent beneficial interest to be issued pursuant to the B&P plan of reorganization and guaranteed or assumed by the NH trustees, and (c) any other securities issued, assumed, or guaranteed by the NH trustees prior to Penn's acquisition of the NH properties which Penn may be required to assume or guarantee under the terms of the

agreement, all in connection with inclusion of NH. Penn also seeks authority, to the extent our approval is required, to enter into confirmatory supplemental agreements with the trustees under NH equipment trusts, the B&P mortgage, the B&P equitable charge indenture or any other indentures in respect of which Penn is authorized to assume obligation or liability in order to evidence Penn's succession to the rights and liabilities under the above security obligations.

Penn's authorized capital stock will be increased from 17,400,000 shares of the par value of $10 per share to 27-million shares upon consummation of the Penn-Central merger. As of August 31, 1966, 13,914,219 shares of Penn's common stock were outstanding. Under the terms of the merger agreement with Central, Penn is required to issue 1.3 shares of its stock for each share of outstanding stock of Central. At August 31, 1966, there were 6,877,859 shares of Central stock outstanding, which, upon consummation of the merger, would require the issuance of 8,941,216 shares of Penn's common stock.

The $23 million in bonds will be secured by a divisional first mortgage. The mortgage is not open-end and does not provide for additional bond issues. It will be secured by all real property acquired by Penn from the NH trustees, including B&P property, except leasehold estates of NH, and will be a first lien on the title to such property. Bonds will be issued in registered form only, in denominations of $100, $500, $1,000 and any integral multiple of $1,000. Holders of bonds may exchange their bonds for bonds of authorized denominations greater than $500, except that the NH trustees may exchange bonds held by them into bonds of any authorized denominations.

The title to property acquired through the B&P reorganization will be subject to a mortgage lien in an amount not exceeding $3,200,000 and also to the "equitable charge" of the certificates of contingent beneficial interest, as provided in the B&P plan of reorganization. The bonds and encumbrances on the property are adequately described in *Boston & P. R. Corp. Reorganization, supra.*

A pro forma general balance sheet of Penn-Central as of September 30, 1966, shows total assets of $4.3 billion of which $395 million are current. Current liabilities are projected at $294 million and total liabilities at $1.9 billion. Shareholders' equity is set forth at $2.4 billion, of which retained income is $1.1 billion.

The projected combined income statement based upon the 9-month period ended September 30, 1966, shows total income of

$138 million, of which net railway operating income is $85 million. Total fixed charges are estimated at $60 million and net income at $70 million. The estimated expenses to be incurred in connection with the issuance of the aforementioned stock and bonds are $69,870.

Upon consummation of the transaction, Penn estimates it will incur annual fixed charges of $2.9 million arising from securities it proposes to issue and those obligations it will assume. These charges could not have an undue adverse effect upon Penn-Central's financial condition.

The security issuances and assumptions of obligation and liability by Penn are vital steps in the acquisition and operation of the properties of the NH by Penn-Central. The precise number of shares of stock and principal amount of bonds to be issued will be affected by price adjustments and other provisions of the purchase agreement.

Without the specific agreements, we cannot determine whether any confirmatory supplemental agreements between Penn and the NH trustees require our approval. Nor, assuming such approval is required, can we properly grant approval of such agreements in advance of their drafting. Accordingly, to this extent we cannot grant the application of Penn in Finance Docket No. 24361. In all other respects the application conforms to the requirements of section 20a.

REQUESTS NOT PASSED ON

U. S. Trust Company.–The United States Trust Company (U. S. Trust), trustee under the Harlem River Division Indenture of First Mortgage, asks us to find that the Harlem River Division Bonds, both as to principal and interest are fully secured by the properties underlying the mortgage. In addition, it requests us either to require Penn-Central to assume all the NH obligations in respect of the bonds or to determine the liquidation value of the properties subject to the mortgage, order a segregation and deposit in the reorganization court registry of an amount of the purchase price equal to that value, and determine that such amount be in the form of cash or first mortgage bonds. As an alternative, U. S. Trust asks us to reject the NH trustees' plan of reorganization and dismiss the reorganization proceeding, unless the trustees file the second step of their plan.

These requests, in large part, have been rendered moot by the filing of the remainder of the NH trustees' plan of reorganization and we will not deal with them until the remainder of the reorganization proceeding is ripe for consideration.

P&W.– P&W requests that amendment No. 1 to the NH trustees' plan of reorganization be disapproved to the extent it rejects the lease with P&W, that the terms and conditions for inclusion of NH in Penn-Central incorporate a condition that P&W be included therein as part of NH, and that P&W be included in the Penn-Central merger as a leased line under the terms and conditions of the existing lease with NH.

The position of P&W stems from the rejection by the NH trustees of the lease with P&W. P&W contends that the lease cannot be rejected. We shall defer passing on this matter until our final decision on the plan of reorganization. Our reservation of jurisdiction herein will permit us to take such action under section 5(2)(d) that we may later find warranted.

ULTIMATE FINDINGS

The increase in total fixed charges which will result from the transaction will not be contrary to the public interest. Appropriate traffic protective conditions have been provided for the benefit of CNJ, Reading, and WM. Conditions have also been imposed for the benefit of NH railway employees.

We have considered all the contentions of the parties and find those not specifically discussed herein to be without merit.

Subject to the various terms and conditions set out in this report, including the appendixes, we find that the purchase by The Pennsylvania New York Central Transportation Company of the properties of The New York, New Haven and Hartford Railroad Company, Debtor, as described herein, and acquisition by The Pennsylvania New York Central Transportation Company, as a result of said purchase, of control through stock ownership or otherwise of other carriers, leases of and rights to operate by contract, or otherwise, the properties of other carriers, and trackage rights over and joint ownership in and joint use of, lines owned or operated by other carriers meet the requirements prescribed by section 5(2) of the Interstate Commerce Act and will enable Pennsylvania New York Central Transportation Company to use service by motor vehicle to public advantage in its rail operations and will not unduly restrain competition. We

further find that upon said purchase Pennsylvania New York Central Transportation Company shall be entitled to operate under the motor carrier operating rights granted to the New England Transportation Company in No. MC-29250.

Pursuant to the provisions of section 5(2)(d) of the act, we find that inclusion of The New York, New Haven and Hartford Railroad Company, debtor, and its affiliates and subsidiaries, in The Pennsylvania New York Central Transportation Company, as a prerequisite to the authorization granted in 327 I.C.C. 475, is required upon the terms heretofore found equitable to all parties involved and as conditioned herein.

We further find that a loan arrangement whereby The Pennsylvania New York Central Transportation Company would make available to the trustees of The New York, New Haven and Hartford Railroad Company the amount of $25 million over a 3-year period commencing with the date of the merger of The New York Central Railroad Company into The Pennsylvania Railroad Company pursuant to the terms and conditions described herein constitute just and reasonable terms and conditions in connection with the inclusion approved herein. The trustees of The New York, New Haven and Hartford Railroad Company, The Pennsylvania Railroad Company, and The New York Central Railroad Company are directed to file with this Commission within 35 days from the effective date of the order herein, a loan agreement, an amendment to the purchase agreement, and an appropriate form of trustees' certificate conforming to the rulings made herein.

We further find, in connection with the inclusion authorized herein, that (a) issuance by The Pennsylvania Railroad Company of 950,000 shares of common stock of the par value of $10 per share and such additional shares as may be made necessary by the purchase price adjustment provisions (sections 8 and 9), and the antidilution provisions (section 20) of the agreement dated April 21, 1966, as modified October 4, 1966, among The Pennsylvania Railroad Company, The New York Central Railroad Company, and the trustees of The New York, New Haven and Hartford Railroad Company, in conformance with the findings and conclusions herein; (b) issuance by The Pennsylvania Railroad Company of $23-million principal amount of 25-year Divisional First Mortgage Bonds, and such larger principal amount of bonds as may result from operations of the purchase price adjustment provisions (sections 8 and 9) of the aforesaid agreement; and (c) the assumption by The Pennsylvania Railroad Company

of obligation and liability in respect of equipment trust obligations guaranteed by The New York, New Haven and Hartford Railroad Company and described in the application in Finance Docket No. 24361, the bonds and certificates of contingent beneficial interest to be issued pursuant to the Boston and Providence Railroad Corporation plan of reorganization, as described in *Boston & P. R. Corp. Reorganization*, 327 I.C.C. 10, and any other securities hereafter issued, assumed, or guaranteed by the trustees of The New York, New Haven and Hartford Railroad Company under section 20a of the Interstate Commerce Act prior to acquisition of the properties of The New York, New Haven and Hartford Railroad Company by The Pennsylvania Railroad Company which the latter may be required to assume or guarantee pursuant to the terms of the aforesaid agreement are (a) for lawful objects within the corporate purposes of The Pennsylvania Railroad Company and compatible with the public interest, which are necessary and appropriate for and consistent with the proper performance by it of service to the public as a common carrier, and which will not impair its ability to perform that service, and (b) reasonably necessary and appropriate for such purposes.

We further find that, pursuant to section 77 of the Bankruptcy Act, the terms for the sale of the said railroad's properties to the Pennsylvania New York Central Transportation Company, originally filed as the first step of the trustees' plan of reorganization are fair and equitable, afford due recognition to the rights of each class of creditors or stockholders, will not materially and adversely affect creditors, does not discriminate in favor of any class of creditors or stockholders, will not be inconsistent with the requirements of the law regarding participation of the various classes of creditors and stockholders, and will otherwise meet the requirements of the Bankruptcy Act, and will be compatible with the public interest.

An appropriate order will be entered.

COMMISSIONER HARDIN did not participate.

APPENDIX A

The New York, New Haven and Hartford Railroad Company table of funded debt[1] for the years 1964, 1965, and 1966

Item	1964	1965	1966
Mortgage bonds:			
Providence Terminal first mortgage			
Harlem River Division first mortgage	$6,648,000	$6,647,000	$6,647,000
N.Y. N.H. & H.R. first or refunded mortgage	76,819,900	76,819,900	76,819,900
N.Y. N.H. & H.R. general mortgage income	52,755,500	52,755,500	52,755,500
Collateral trust notes[2]	10,628,284	6,275,320	3,917,370
Equipment obligations	21,358,644	21,034,546	[3]17,290,250
Trustees securities	8,000,000	12,500,000	12,500,000
Promissory notes	12,400,000	12,400,000	12,872,100
Other obligations	609,725	609,725	609,725
Total	189,220,053	189,041,991	182,911,845

[1]Includes debt in default; excludes debt due within 1 year.

[2]Obligations are being liquidated in accordance with court order No. 347 dated December 30, 1965.

[3]Includes $365,019 in conditional sale contracts (schedule 218, page 234, Rail Form A, 1966).

Source.—NHI-30, table 12; schedule 218, Rail Annual Report Form A for the year ended December 31, 1966—The New York, New Haven and Hartford Railroad Company.

APPENDIX B

The New York, New Haven and Hartford Railroad Company income accounts for the years 1965 and 1966

Income accounts	1966	1965
Railway operating revenues	$125,645,075	$121,484,147
Railway operating expenses	115,436,383	113,983,049
Net revenue	10,208,692	7,451,098
Railway tax accruals	9,168,290	9,150,894
Railway operating income	1,040,402	(1,699,796)
Total rent income	1,442,949	1,696,152
Total rents payable	(15,526,885)	(16,004,000)
Net rents	(14,083,936)	(14,307,868)
Net railway operating income	(13,043,534)	(16,007,664)
Other income:		
From nonoperating property	5,459,625	5,436,609
other income	5,175,135	4,177,692
Total income	(2,408,774)	(6,393,363)
Miscellaneous deductions	(2,950,047)	(2,029,087)
Income available for fixed charges	(5,358,821)	(8,422,450)
Fixed charges:		
Rent for leased roads and equipment	(801,158)	(801,155)
Fixed interest not in default	(1,754,689)	(1,761,621)
Interest in default	(3,355,294)	(3,971,440)
Interest on unfunded debt	(47,459)	(67,779)
Amortization of discount on funded debt	(27,602)	(36,944)
Total fixed charges	(5,986,202)	(6,640,939)
Income after fixed charges	(11,345,023)	(15,063,389)

( ) Deficit.

Source.—Rail Form A for the years ended December 31, 1965 and 1966—The New York, New Haven and Hartford Railroad Company.

APPENDIX C

The New York, New Haven and Hartford Railroad Company comparative general balance sheet as of December 31, 1965 and 1966

Account	1965	1966
Assets		
Cash	$5,486,116	$5,067,441
U. S. Treasury obligations	----------	996,605
Other current assets except material and supplies	10,832,925	9,901,764
Material and supplies	4,202,354	3,951,619
Total current assets	20,521,395	19,917,429
Special funds (including principally funds in escrow and proceeds from sale of property)	13,206,750	12,289,758
Investments (including affiliated companies)	19,813,258	19,726,479
Total transportation property less recorded depreciation and amortization	308,120,214	293,589,179
Miscellaneous physical property less recorded depreciation	28,346,335	28,680,117
Other assets and deferred charges	5,588,516	6,433,507
Total assets	395,596,468	380,588,469
Liabilities and shareholders' equity		
Accrued accounts payable	13,130,107	13,439,393
Other current liabilities	16,320,399	14,317,474
Total current liabilities	29,450,506	27,756,867
Debt due within 1 year (including equipment obligations)	7,755,330	5,744,286
Long-term debt (including $149 million in default)	189,041,991	182,911,845
Casualty reserves (including over $7 million in injury claims)	7,150,518	8,071,217
Interest in default	19,804,126	23,159,420
Other liabilities and deferred credits (including an excess of $22 million in disputed per diem)	67,602,369	69,498,219
Total other liabilities and deferred credits	291,354,334	289,384,997
Total liabilities	320,804,840	317,141,864
Shareholders' equity:		
Capital stock (including common and preferred)	156,462,141	156,461,941
Capital surplus	1,500	1,700
Retained income (deficit)	(81,672,013)	(93,017,036)
Total shareholders' equity	74,791,628	63,446,605
Total liabilities and shareholders' equity	395,596,468	380,588,469

Source.–Rail Form A for the year ended December 31, 1966–The New York, New Haven and Hartford Railroad Company.

APPENDIX D

The New York, New Haven and Hartford Railroad Company condensed income statement for the years 1961-66

Year	Net railway operating deficit	Income (deficit) before fixed charges	Net income (deficit) after fixed charges and other deductions
		(000 omitted)	
1961	($19,577)	($11,952)	($19,550)
1962	(11,514)	(55,083)	(12,741)
1963	(10,090)	(4,884)	(12,264)
1964	(17,056)	(8,826)	(15,268)
1965	(16,008)	(8,422)	(15,068)
1966	(15,044)	(5,359)	(11,345)

Source.—NHI-30, table 1; schedule 300, Rail Form A for the year ended December 31, 1966—The New York, New Haven and Hartford Railroad Company.

The New York, New Haven and Hartford Railroad Company condensed balance sheet as of December 31, 1961 to 1966, inclusive

Year	Total assets	Total liabilities	Shareholders' equity
		(000 omitted)	
1961	$420,205	$293,934	$126,271
1962	409,838	296,303	113,535
1963	403,168	301,898	101,270
1964	394,052	308,045	86,007
1965	395,596	320,805	74,791
1966	380,588	317,141	63,447

Source.—NHI-30, table 2, page 1; schedule 200, Rail Form A for the year ended December 31, 1966—The New York, New Haven and Hartford Railroad Company.

APPENDIX E

Pennsylvania New York Central Transportation Company combined income statement of The Pennsylvania Railroad Company and The New York Central Railroad Company

Period	Net railway operating income	Income available for fixed charges	Net income after fixed charges
		(000 omitted)	
Year ended December 31, 1965	$95,851	$153,806	[1]$75,416
Nine months ended September 30, 1966	84,897	130,268	69,955

[1]Excludes $8 million estimated annual savings to be realized from merger before Federal income taxes.

Source.–NHI-72, page 24.

Pennsylvania New York Central Transportation Company pro forma general balance sheet after giving effect to merger of The New York Central Railroad Company into The Pennsylvania Railroad Company September 30, 1966

ASSETS		
Current assets		$394,794,940
Special funds		33,406,067
Investments		1,095,839,859
Total properties less recorded depreciation and amortization		2,713,751,732
Other assets and deferred charges		33,858,208
Total assets		4,271,650,806
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		294,465,706
Long-term debt due within 1 year		72,146,925
Long-term debt due after 1 year		1,247,293,020
Reserves		50,560,532
Other liabilities and deferred credits		204,183,520
Shareholders' equity:		
Capital stock (22,860,379 shares)	$228,603,790	
Capital surplus	1,030,906,889	
Total retained income	1,143,490,424	
Total shareholders' equity		2,403,001,103
Total liabilities and shareholders' equity		4,271,650,806

Source.–NHI-72, page 25.

APPENDIX F

The Pennsylvania Railroad Company condensed consolidated income statement[1] for the years 1961 through 1965

Year	Income before fixed charges	Minority interest in income of subsidiaries	Net income after fixed charges, other deductions, and minority interests
		(000 omitted)	
1961	$50,015	----------	$12,334
1962	49,378	----------	12,500
1963	60,421	----------	24,054
1964	104,782	$4,922	60,097
1965	122,002	6,602	70,118

Source.—NHI-72, page 11.

The Pennsylvania Railroad Company condensed consolidated balance sheet[1] as of December 31, 1961 to 1965, inclusive

Year	Total assets	Total liabilities	Minority shareholders' equity of consolidated companies[2]	Penn R. shareholders' equity[3]
		(000 omitted)		
1961	$2,873,487	$1,059,620	$84,278	$1,749,589
1962	2,846,822	1,011,989	83,664	1,751,169
1963	2,845,851	1,000,714	82,974	1,762,193
1964	3,265,048	1,227,856	253,672	1,783,520
1965	3,603,319	1,504,375	298,880	1,800,066

[1]For the years 1961 to 1965 inclusive, includes results of The Pennsylvania Railroad Company, companies (except the Long Island R. Co.), the common stocks of which are owned 100 percent, directly or indirectly, and companies operated uunder agreements. For 1964 and 1965, as a result of change in basis of consolidations, includes results of Pennsylvania Railroad Company and subsidiaries controlled by The Pennsylvania Railroad Company or its subsidiaries through ownership of more than 50 percent of the voting stock at December 31, 1965.

[2]Includes equity of minority shareholders in consolidated subsidiaries; in the case of 1964 and 1965 only; also includes excess of net assets of consolidated subsidiaries over investment.

[3]Except for the years 1964 and 1965, includes the net amount by which system equity in net assets (at date of acquisition) of companies consolidated exceeds the related investment therein.

Source.—NHI-72, pages 9 and 10.

APPENDIX G

The New York Central Railroad Company condensed consolidated income statement[1] for the years 1961 through 1965

Year	Net railway operating income	Income before fixed charges	Minority interest in income of subsidiaries	Net income (deficit) after fixed charges, other deductions and minority interests
		(000 omitted)		
1961	$11,158	$38,754	$4,112	($10,334)
1962	28,512	45,540	4,863	2,210
1963	38,901	56,162	5,471	16,117
1964	54,542	78,923	5,941	37,453
1965	68,598	93,978	4,236	54,203

Source.—NHI-72, page 14.

The New York Central Railroad Company condensed consolidated balance sheet[1] as of December 31, 1961 to 1965, inclusive

Year	Total assets	Total liabilities	Minority shareholders' equity—con subs	Shareholders' equity—NY Central[2]
		(000 omitted)		
1961	$2,442,612	$1,106,672	$78,504	$1,257,436
1962	2,382,112	1,046,981	77,424	1,257,707
1963	2,361,641	1,016,754	80,936	1,263,951
1964	2,384,693	1,015,035	81,038	1,288,620
1965	2,386,345	1,000,219	65,766	1,320,360

Source.—NHI-72, page 13.

[1]Includes the accounts of The New York Central Railroad Company and subsidiary companies of which Central controlled, directly or indirectly, in excess of 50 percent of the equity stock.

[2]Includes excess of net assets (at acquisition) of consolidated subsidiaries over carrying value of investment.

APPENDIX H

The New York, New Haven and Hartford Railroad Company interest in deault for the years 1964, 1965, and 1966

	1964	1965	1966
Mortgage bonds:			
Harlem River Division first mortgage	$1,133,843	$1,412,487	$1,694,985
N.Y. N.H. & H. R. first and refunded mortgage	12,291,184	15,363,980	18,436,776
Collateral trust bonds[1]	2,263,706	----------	----------
Equipment obligations	9,511	9,511	9,511
Promissory notes	2,343,139	2,963,139	2,963,139
Other obligations	55,009	55,009	55,009
Total[2]	18,096,392	19,804,126	23,159,420

[1]Obligations are being liquidated in accordance with court order No. 347 dated December 30, 1965. Interest accrued or to accrue prior to January 1, 1968 has been waived. (Notes and remarks—schedule 218, page 233, Rail Form A, 1965).

[2]Excludes $7,121,994 in accrued interest on New York, New Haven and Hartford Railroad Company general income mortgage bonds (Note A—schedule 225, page 243, Rail Form A, 1966).

Source.—Rail Form A for the years ended December 31, 1964, 1965, and 1966—The New York, New Haven and Hartford Railroad Company.

APPENDIX I

Upon inclusion of the NH in the transaction authorized by the Interstate Commerce Commission in Finance Docket No. 21989:

1. Penn-Central, WM, Reading, and CNJ, as to traffic moving to and from all stations on or reached via the lines of the NH, to or from stations on the lines of WM, Reading, and CNJ, shall with respect to each other maintain and keep open existing or comparable routes and channels of trade in full vigor as fast competitive service routes via existing or comparable junctions or gateways, unless and until otherwise authorized by the Interstate Commerce Commission.

2. The present neutrality of handling traffic inbound and outbound by NH shall be continued by Penn-Central, insofar as such matters are within its control, so as to permit equal opportunity for service to and from the lines of WM, Reading, and CNJ without discrimination as to routing or movement of traffic and without discrimination in the arrangement of schedules or otherwise. Likewise, the present neutrality of handling traffic inbound and outbound by WM, Reading, and CNJ shall be continued so as to permit equal opportunity for service to and from the lines of NH included in Penn-Central without discrimination as to routing or movement of traffic and without discrimination in the arrangement of schedules or otherwise.

3. The present traffic and operating relationships existing between NH, on the one hand, and WM, Reading, and CNJ, on the other, shall be continued insofar as such matters are within the control of Penn-Central, on the one hand, and WM, Reading, or CNJ, on the other.

4. Insofar as such matters are within its control, Penn-Central shall, as to the lines of NH included in the transaction authorized in Finance Docket No. 21989, accept, handle, and deliver all cars inbound and outbound, loaded and empty, without discrimination in service as between cars destined to or received from WM, Reading, and CNJ, and irrespective of destination or route of movement. Likewise, WM, Reading, and CNJ shall accept, handle and deliver all cars inbound and outbound, loaded and empty, without discrimination in service as between cars destined to or received from the lines of NH included in the transaction authorized in Finance Docket No. 21989 and carriers competing with said latter lines of Penn-Central, and irrespective of destination or route of movement.

5. Penn-Central shall not do anything to restrain or curtail the right of industries now located on the lines of NH to route traffic over existing or comparable routes and gateways in connection with WM, Reading, or CNJ. Likewise, neither WM, Reading, nor CNJ shall do anything to restrain or curtail the right of industries now located on its lines to route traffic over

existing or comparable routes and gateways in connection with the lines of the NH included in the transaction authorized in Finance Docket No. 21989.

6. Insofar as such matters are within their control, Penn-Central, on the one hand, and WM, Reading, and CNJ, on the other, shall cooperate with each other and each shall use its best efforts with its connections to obtain similar cooperation in order to continue the NH-CNJ-Reading-WM route as a competitive service route for the movement of freight traffic between points located on or beyond NH's lines and points located on or beyond WM's, Reading's, and CNJ's lines, endeavoring at all time to improve such service and maintaining at least the same standards of service as prevail on the date of the consummation of the Penn-Central merger; and neither WM, Reading, or CNJ, on the one hand, nor Penn-Central, on the other, shall, without the written consent of the other, make any substantial change in train schedules or take any other action, the effect of which would be to increase the time in transit via the aforesaid routes, or to otherwise adversely affect the standards of service; provided, however, that if all other obligations of these conditions have been complied with, this paragraph shall not be construed to require the maintenance of train service or schedules if revenues from operations via the aforementioned joint routes during any 6 months' period have been insufficient to cover out-of-pocket costs.

7. With respect to traffic presently handled jointly by the NH, on the one hand, and the CNJ, Reading, or WM, on the other, Penn-Central, WM, Reading, and CNJ will, insofar as such matters are within their control, continue to publish or concur in publication of rates so that rates to or from points on or reached via WM, Reading, or the CNJ routes will always be competitive with other routes and as to the aforesaid traffic they shall also concur in divisions of such rates under the established bases of divisions, and in the event of any reductions in joint rates proportionate reductions shall be made in the divisions of Penn-Central.

8. Insofar as such matters are within their control, Penn-Central, on the one hand, and WM, Reading, and CNJ, on the other, will cooperate in continuing the solicitation of that traffic in which the NH now participates over routes via WM, Reading, or CNJ having competitive rates and services.

9. Any party or person having an interest in the subject matter may at any further time make application to the Commission for such modification of the above conditions, or any of them, as may be required in the public interest, and jurisdiction shall be retained by the Commission to reopen the proceeding on its own motion for the same purpose.

10. These conditions shall be contingent upon and shall take effect on the date of consummation of the Penn-Central merger authorized in Finance Docket No. 21989 and upon their acceptance by WM, Reading, and CNJ, evidenced in writing to the Commission.

F-9511

INTERSTATE COMMERCE COMMISSION

FINANCE DOCKET NO. 21989[1]

PENNSYLVANIA RAILROAD COMPANY–MERGER–NEW YORK CENTRAL RAILROAD COMPANY

Decided November 25, 1968

1. On reconsideration, reports and orders of November 16, 1967, and March 1, 1968, reinstated and affirmed, as modified, with respect to property valuation and other matters. Prior reports 327 I.C.C. 475, 328 I.C.C. 304, 330 I.C.C. 328, 331 I.C.C. 643, and 331 I.C.C. 754.
2. Inclusion of the New York, New Haven & Hartford Railroad Company in the Penn Central system as of January 1, 1969, approved and directed.
3. Inclusion of Providence & Worcester Railroad Company and the Norwich & Worcester Railroad Company in the Penn Central system as leased lines, authorized and directed. Conditions prescribed.
4. Plan of reorganization of the New York, New Haven & Hartford Railroad Company modified and approved.

Appearances as shown in prior reports and *Owen F. Clarke, Jr., William G. Bardel,* and *Harvey J. Goldschmid* for applicants.

Michael Alexander, Craig S. Bamberger, Kellog W. Beck, James S. Hostetler, John Hupper, Robert K. Killian, Homer Kripke, Norman H. Lane, William J. Lynch, Peter MacDougall, Walter H. Mayo III, Douglas Mercer, Elliott L. Richardson, George Schacht, Oscar M. Shaw, and *Sidney Weinberg,* for interveners.

Edwin M. Zimmerman for United States Department of Justice.

Stanford G. Ross, Peter S. Craig, and *Stephen J. Gross* for United States Department of Transportation.

Bernard A. Gould and *Ellis V. Gregory* for Bureau of Enforcement, Interstate Commerce Commission.

FOURTH SUPPLEMENTAL REPORT OF THE COMMISSION ON RECONSIDERATION AND FURTHER HEARING

[1]Embraced herein are Finance Docket No. 21990, Pennsylvania Railroad Company Stock Issuance; Finance Docket No. 24361, Pennsylvania Railroad Company Securities and Assumption of Obligations, and Finance Docket No. 21669, New York, New Haven & Hartford Railroad Company Reorganization.

BY THE COMMISSION:

The subject of these consolidated proceedings is the inclusion, under section 5(2)(d) of the Interstate Commerce Act, of the financially-distressed New York, New Haven and Hartford Railroad Company, Richard Joyce Smith and William J. Kirk, trustees (herein NH), in the newly-merged Penn Central Company (Penn Central). The Penn Central merger[2] was consummated on February 1, 1968, pursuant to the joint application filed by the merging carriers, The Pennsylvania Railroad Company (Penn) and The New York Central Railroad Company (Central). New Haven has been a debtor in reorganization since July 1961 under section 77 of the Bankruptcy Act (11 U.S.C. 205), and has since that time remained under the jurisdiction of the United States District Court for the District of Connecticut sitting as a reorganization court.

In approving the Penn Central merger, we attached certain conditions which required, among other things, that the merging companies include NH and its affiliates and subsidiaries upon such fair and equitable terms as the parties may agree, subject to the approval of this Commission and the reorganization court, or, if the parties failed to reach agreement, upon such fair and equitable terms and conditions as the Commission, with the court's approval, might impose. Consummation of the merger, we stated, would indicate the full and complete assent by Penn and Central to these and other requirements, and we retained jurisdiction over the transaction for these and other purposes.

These proceedings also involve the development of a plan of reorganization of NH under section 77 of the Bankruptcy Act. The NH trustees submitted a plan under which the merging companies would purchase substantially all of the assets of NH and assume certain of its obligations. In the *inclusion* report we considered certain applications for authority to issue the securities and assume the obligations and liabilities necessary to effectuate the purchase and inclusion, and certain interim arrangements under which the merging companies, and later Penn Central, through a loan fund, would make cash available for the continued operation of NH pending inclusion, and Penn Central would absorb a portion of NH's operating losses.

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[2] At 327 I.C.C. 475, decided April 6, 1966 (the *merger* report). Subsequent reports (1966) at 328 I.C.C. 304 (*reconsideration* report) (1967), at 330 I.C.C. 328 (*supplemental* report) and 331 I.C.C. 643 (*inclusion* report), and (1968) at 331 I.C.C. 754 (*third supplemental* report).

By our decision in the *inclusion* report, we authorized and directed the inclusion in Penn Central of NH and its affiliates and subsidiaries upon terms and conditions which we found to be equitable to all parties involved, and we authorized the issuances of stock and securities, and the assumptions of liabilities, necessary in connection therewith. We also approved the first step of a plan of reorganization of NH and certified the same, pursuant to section 77(d) and (e) of the Bankruptcy Act, to the reorganization court. Consideration of the second step of the reorganization plan and certain other issues was deferred,[3] and, as here particularly pertinent, we denied a request by Erie Lackawanna Railroad Company (EL), a petitioner herein, for the imposition of certain conditions for the protection of its traffic from the effects of the inclusion of NH.

Appeals from our conclusions and findings in the *inclusion* and *third supplemental* reports were taken by certain creditor interests[4] of NH and consolidated in an action before a statutory three-judge court, the United States District Court for the Southern District of New York (the three-judge court). EL intervened as a plaintiff to appeal our denial of its protective conditions. By opinion and order dated July 10, 1968,[5] the three-judge court vacated our *inclusion* report and order and remanded the matters to us for further consideration and proceedings in the light of the court's conclusions. By memorandum opinion, dated August 5, 1968, the three-judge court denied a motion by Penn Central for reargument. Shortly thereafter, by an opinion entered August 10, 1968,[6] the reorganization court declined to approve the first step of the reorganization plan referred to it and remanded

[3] A public hearing on the second step (Amendment No. 2 to the trustees' plan) was held and briefs and replies were filed. By order of October 5, 1967, we omitted the examiner's report, and that record was certified to us for initial decision and subsequently incorporated into the record of the present proceeding.

[4] The New York, New Haven and Hartford Railroad Company, First Mortgage 4 percent Bondholders Committee (the Committee); The Chase Manhattan Bank, N.A., as trustee under the General Income Mortgage of the New York, New Haven and Hartford Railroad Company (Chase); Manufacturers Hanover Trust Company, as trustee under the First and Refunding Mortgage of the New York, New Haven and Hartford Railroad Company (Manufacturers); United States Trust Company of New York, as trustee under the New York, New Haven and Hartford Railroad Company's Harlem River Division Indenture of First Mortgage (US Trust); and Oscar Gruss & Son (Gruss).

[5] *New York, New Haven and Hartford Railroad Company, First Mortgage 4 percent Bondholders Committee, et al. v. United States of America and Interstate Commerce Commission, et al.*, 289 F. Supp. 418 (S.D.N.Y., 1968).

[6] *In re New York, New Haven and Hartford Railroad Co.*, 289 F. Supp. 451 (D. Conn., 1968).

the matter to us for further proceedings and modification of the plan in accordance with the court's views.

Of particular significance, in the present posture of these proceedings, is the reorganization court's finding that:

> the continued erosion of the Debtor's estate from operational losses after the end of 1968 will clearly constitute a taking of the Debtor's property and consequently the interests of the bondholders, without just compensation. It is therefore constitutionally impermissible, and obviously no reorganization plan which calls for such a taking can be approved.

The court went on to state that there is no reason why Penn Central should not "take over the New Haven at the beginning of 1969," and indicated that the bondholders may be required to continue to bear a share of NH's operating losses until December 31, 1968, "to afford the Commission an opportunity to consider and rule upon the issuance of an order to the Penn Central physically to take over and commence operating the New Haven Railroad not later than January 1, 1969, leaving the price and the other terms of the inclusion to be determined later." The court made it clear that:

> If the Commission decides not to issue such an order this court will reluctantly be forced to entertain a motion to dismiss the reorganization proceedings.

The urgencies of the situation were emphasized by the three-judge court as well, which stated:

> We urge the Commission and all parties to proceed with the utmost expedition. To the extent that new testimony is required, this should be held to a minimum; we do not mean by this opinion that parties who had a full opportunity to present evidence must be given a new turn.

Both courts established guidelines, but preserved the maximum flexibility of the remanded proceedings. In the light of such remand, we issued our order of August 26, 1968, which reopened the prior proceedings for reconsideration, and consolidated them with the proceedings involving the second step of the plan of reorganization. We provided an expedited procedure for further hearing in these matters, and for due and timely execution of our functions we required the omission of an examiner's report and recommended order and certification of the record to us for initial decision.

Petitions were filed by the trustees and by several creditor interests of NH seeking a severance of the issue of immediate

inclusion of NH and requesting an order requiring inclusion by January 1, 1969, with partial payment therefor by Penn Central. The petitions were supported by several New England States, parties herein, and others, and opposed by Penn Central. By our order of September 27, 1968, we denied the petitions, indicating in our order, however, that further consideration would be given to this matter should it appear necessary in the public interest. In a public statement concurrently issued, the Commission's chairman emphasized that the expedited procedures prescribed were for the purpose of bringing about a decision on all issues by early December, and to make possible inclusion of NH by January 1, 1969. In this connection, Penn Central and NH were urged to commence promptly the arrangements for an orderly transfer of the NH operations to Penn Central.

Under the expedited procedures, hearings in these matters commenced October 7, 1968, and were completed October 15, 1968. The following day, acting on a petition by NH for authority to make further borrowing from the Penn Central loan fund, the reorganization court issued its order permitting New Haven to take down an additional $4 million from Penn Central under the loan arrangement approved in the *inclusion* report, and to deposit the same in the court's registry. The trustees estimated that the $4 million take-down would enable NH to continue its operations through the remainder of 1968.

The parties have filed briefs and rebuttal briefs, as provided in our August 26 order, and have stated their respective positions as to whether they favor inclusion of NH by January 1, and if so, by what method and upon what terms and conditions. Several parties have requested oral argument, which at this stage is unnecessary and unwarranted, particularly in view of the voluminous record made at the hearings, the extensive briefs filed, and the expeditious handling necessitated by NH's dwindling operating funds. Similarly, oral argument requested by the trustees on the so-called "second step" of the reorganization plan is unnecessary. Several parties also have challenged various evidentiary rulings of the hearing examiner. We have reviewed the entire record and find that the parties were afforded full and fair opportunity to present their evidence and make their positions known under the framework of our order of August 26, 1968. To the extent that evidence was proffered on the processing time of possible abandonment proceedings involving NH, such matters are within our knowledge and evidence thereon was unnecessary. We therefore

sustain the examiner's rulings and deny the requests for oral argument.

While preserving to us the opportunity to develop other theories for the valuation of NH's assets, both courts have stressed liquidation value. We are instructed to determine each element of this value. The specific issues remanded to us are relatively few in number and will be individually discussed. Where the courts have sustained our prior reports, we adopt and reaffirm their contents unless expressly modified herein; only a few of the matters on which we have been sustained will receive any comment in this report.

LIQUIDATION VALUE OF THE NH ASSETS

In the *inclusion* report, we found that the net liquidation value of NH's assets was about $125 million. Each of the figures necessary to a computation of this net amount was contained in that report, except a figure of $3 million for 1966 depreciation which was referred to only in general terms. The courts have held that we erred in certain specifics in computing the liquidation value. Each of these will be discussed in light of the new record.

Grand Central Terminal properties.—In the *inclusion* report, we valued NH's interest in the Grand Central Terminal properties at $13 million. We reached this valuation by averaging the $5 million "nuisance value" Penn Central had assigned NH's interest on the theory NH had no valuable property interest and a figure of $20 million, which we believed was NH's maximum potential interest in the properties. The maximum was based on the theory that: (1) NH might be able to establish an interest in "excess income" from the properties after all terminal expenses; (2) the measure of that interest would be NH's car-user percentage[7] of the excess; and (3) NH's share should be capitalized at 8 percent. Both the three-judge court and the reorganization court have held that we erred in our valuation.

Both courts agree that NH has a valuable interest in these properties that would survive liquidation of the railroad. They agree that NH has an interest in the excess income after payment of all terminal expenses, and that the measure of that

[7]Penn Central and NH share terminal expenses and deficits on the basis of their respective car entries into the terminal. NH's car user percentage in recent years has been about 41 percent.

interest is 50 percent or an equal division with Penn Central of such excess. They also sustain our use of a capitalization rate of 8 percent.[8] We accept these rulings, and these particular matters need not be considered further.

By order dated April 8, 1968, the reorganization court referred the matter of valuation of the Grand Central Terminal properties to a special master for a legal appraisal of the rights and interests of NH therein. After holding hearings, the special master reported his findings to the reorganization court in reports dated June 17, 1968 and July 22, 1968. The second hearing before the special master was concerned primarily with the future prospects of the Grand Central Terminal properties. The special master stated in his second report that in his view the Commission had failed to give sufficient weight to the prospects for increased income. The record of that hearing was incorporated into the record of the reopened proceeding.

A preliminary matter presented by the second report of the special master relates to what accounts are relevant to a computation of profit or loss in past years. No less than four sets of books have been kept regarding the relevant income and expenses. NH has followed a modified accrual method which it combines with retirement accounting for the capital expenditures of the hotels. Penn Central follows depreciation accounting with respect to these capital expenditures. Penn Central also keeps a so-called "Terminal Account" on a cash basis in which it computes the profit or loss from all terminal income and expenses. Penn Central's subsidiary, Realty Hotels, Inc., also keeps its own books. The annual figures resulting from these different accounts and accounting methods will agree, if ever, only over a period of many years.

The special master would use the NH figures to the exclusion of all others. We disagree. The terminal agreements on their face require deduction of capital expenditures before computing excess income. The "Terminal Account" figures best reflect capital expenditures likely to be incurred in the future,[9] and afford the best basis for forecasting future excess income. NH's retirement or replacement accounting method postpones charges for loss resulting from depreciation until such loss is fully realized. NH's method could leave much of the capital expenditures of the hotels in investment until the hotels are torn down, and,

[9]This subject matter is discussed in greater detail under "Hotel income," *infra.*

[8]We note in passing that the evidence taken before the special master suggests the correctness of at least an 8 percent figure.

therefore, not reflect the full expense.[10] Net accruals described later herein of $482,000 of hotel income earned but not paid over, however, should be added before computing prior income averages from this source, for an accurate picture of actual earnings.

Penn Central would have us ignore the subaccounts of the "Terminal Account" and simply average the excess income experienced in the 1964-1967 period. This approach is unfair to the NH creditors. Although we adopt that method for some subaccounts, the method if used for all the subaccounts would unfairly understate foreseeable excess income.

The reorganization court requested us to decide "what value, if any, attaches" to NH's right to free use of Grand Central Station. Station expenses are a first charge on all terminal income, and such expenses annually amount to about $13.6 million. NH's 41 percent share of those expenses amounts to $5.6 million. In liquidation the right to free use of the terminal would have no value to NH unless there were a buyer willing to pay for such use.

The only potential buyer in sight is the State of New York which would not need to bid for free use of the terminal. First, the State could seek to be relieved of the heavy tolls and interest on capital expenditures which NH now pays Penn Central. Second, it could offset the annual tax forgiveness against the current operating expenses of the terminal. Hence, such free use is valueless. We agree with the three-judge court that no such buyer is in sight, that the State of New York would need to pay for only the net cost of operating into the terminal,[11] and that this is indeed an "extravagant claim" of the creditors.

Bearing in mind that NH's interest is in excess income, we next review the past and potential performance of the Terminal

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[10] In *Telephone and Railroad Depreciation Charges*, 177 I.C.C. 351 (1931), we prescribed depreciation accounting in lieu of other options, such as retirement accounting, for many classes of road property in order to bring about more uniformity and equalization in this expense. Our order did not become effective for class I railroads until January 1, 1943. See our 55th Annual Report, pages 54-55; 56th Annual Report, pages 52-53.

[11] Although NH's right to excess income could survive liquidation, it does not follow that free use of the terminal would be assignable. The bondholders' "free-use" argument is in a real sense no more than an attempt to revive their argument, rejected by us and the courts, that NH is entitled to one-half interest in the terminal income *before* terminal expenses.

Account. The major controversy between the parties is over the future revenue. We begin with a brief discussion of the expense side.

Terminal expenses.—The "Total Expenses" shown in the Terminal Account (exclusive of charges directly relating to the hotels), declined from $18 million in 1960 to $13.6 million in 1967. Since 1960, operating expenses have declined from $11.5 million to about $9.5 million. The decline occurred through reductions in the cost of producing power, the number of employees, and the amount of maintenance such as station maintenance.[12] Penn Central described the future wage increases that would occur under existing agreements. Its testimony shows that it can now hope to absorb no more than one-half of these increases. Of the $9.5 million of operating expenses, $6.5 million are labor or labor-related. Substantial reductions in force have already occurred; reductions of the prior magnitude cannot continue. In addition, the reduction in maintenance amounted to $400,000 annually; we would expect maintenance costs to increase, rather than decline, in the future.

Penn Central projected an annual increase in labor costs of about $360,000 for terminal employees. It further projected an ability to absorb $180,000 of this increase. The carrier's projection of annual increased costs of $180,000 is reasonable. The "Total Expenses" of the terminal averaged $13,670,000 in the period 1964–1967. We will employ the figure $13,850,000 in computing future excess income.

Office building income.—The income in this category has increased substantially since 1960. From $3,443,612 in that year, this income increased to $5,644,163 in 1967. Further increases are in prospect; the Committee properly states that percentage rentals and escalation clauses alone on certain properties will increase income by at least another $109,000 over 1967 income.

The major difference between the parties in this category centers around the proposed lease of air rights over Grand Central Station to construct the so-called "Tower" building. The special master stated that, "whether the opposition to its construction will succeed is not presently known, but it would seem to me that the probabilities are in its favor." Penn Central claims that the proposed building is too speculative and uncertain

[12] A substantial reduction of $2.5 million in real estate and franchise taxes also occurred in the total expense figure.

to serve as the basis for a forecast of increased future excess income.

The facts, which are essentially undisputed, are as follows:

1. A responsible tenant has signed an agreement to lease the space over the station for 75 years at a net rental that begins at $1 million per year in the first, second, and third years, and increases to $3 million per year in the fourth year and thereafter. The rent would be offset in part by the tenant's right to receive rentals for certain concessions in the Terminal which now aggregate $700,000 per year. The long-range rental would be a net advantage to the NH and the Penn Central of about $2.3 million per year, or in "certain favorable circumstances" $3 million.

2. The lease agreement is conditioned upon obtaining the approval of the Landmarks Preservation Commission of the City of New York by no later than January 1, 1970. While other approvals are necessary, the approval of the Landmarks Preservation Commission is the only one whose absence voids the lease. There has been a proposed zoning change having future effect, and opposition within the city government to the proposed building.

3. Penn Central has brought a proceeding to contest the designation of the terminal as a landmark; this proceeding has been held in abeyance. Penn Central requested a "certificate of no exterior effect" from the Landmarks Preservation Commission. The certificate was denied on September 20, 1968, and no appeal is planned. Penn Central may still apply for a "certificate of appropriateness."

The first question raised by these limited facts is whether the proposed building is so speculative that no value can be assigned to it. We here think the NH creditors are entitled to the benefit of the doubt; NH has a valid claim which should be reflected in our valuation results. The special master appropriately remarked:

> The Grand Central Station is not proposed to be removed. It is doubtful that the City could insist upon its being maintained at Penn Central's expense as a memorial to the golden age of railroading.

Moreover, Penn Central has several remedies before the Landmarks Preservation Commission which it has refrained from pursuing. In our judgment it is probable that the building will eventually be constructed, but the administrative and court proceedings reflect a substantial wait until the building is income-producing. The building itself may not be constructed for 5 years, and, if so, it would not reach its maximum rental of $2.3 million until the ninth year.

We believe the fairest resolution of the valuation of this potential is to value the maximum rental of $2.3 million, substantially discounted for its distant future effect on excess income. Certificates of contingent beneficial interest (CCBI's), suggested by the creditors, would not be appropriate, since (1) the controversy over value should be settled, (2) such controversy is susceptible of a reasonable settlement, and (3) where CCBI's have been used (as in the B&P reorganization) they have not removed the need to value the interest as we have discovered in the present case. For a valuation as of December 31, 1966, a discount over at least a 10-year period is reasonable. Therefore, a discount factor[13] of 0.558 will be used, which means that as of 1966, the value of the proposed Tower building is $1.28 million per year.

Hotel income.–The hearings before the special master and before the Commission's hearing examiner produced a large amount of evidence relating to the future prospects of the hotels in the Grand Central Terminal area. There are five hotels, namely the Waldorf Astoria, Biltmore, Barclay, Commodore and the Roosevelt. They are relatively old and established hotels whose income has increased after a decline in the early 1960's. The Terminal Account showed the following hotel income after capital expenditures and before deduction of the Waldorf repayments of capital to each carrier in the past 4 years:

1964	$7,479,536
1965	6,891,282
1966	6,447,875
1967	7,103,301

The 1964–1967 average was about $7,101,000, after inclusion of $482,000 of accrued but unpaid hotel income shown of record.

Before proceeding further, we note that the special master stated that "an amount just short of $800,000 was accrued but not paid over in cash in 1967 by the Barclay, Commodore and Roosevelt." He did not take into account the results for 1966, nor did he give any weight to the testimony that Penn Central was entitled to reimbursement for an advance made in 1967 by which it and NH obtained an early cancellation of the Commodore lease. Our estimate of the accrued and unpaid hotel income shows a net balance due the Terminal Account of $482,000 comprised of the following 1966 and 1967 balances for each of the three hotels:

[13] This and other discount factors used in this report are taken from a standard table of factors used in various exhibits such as that shown in Simpson, Perenian, and Crenshaw's, *Mathematics of Finance*, 2d Ed., Prentice-Hall, Inc. (1941).

Line No.		Barclay		Roosevelt		Commodore		
		1967	1966	1967	1966	1967	1966	
		Thousands		*Thousands*		*Thousands*		
1	Gross earnings	$2,405	$1,953	$1,875	$1,438	$834		UNDER LEASE
2	Less steam and electricity[1]	129	129	101	101	80		
3	Capital expenditures	2,276	1,824	1,774	1,337	754		
		578	616	519	631	546		
4	Credited to Terminal Account	1,698	1,208	1,255	706	208		
		1,321	1,353	1,077	717	0		
5	Less advance[2]	377	(145)	178	(11)	208		
		------	------	------	------	125		
6	Balance due Terminal Account	377	(145)	178	(11)	83		

[1]Steam and electricity provided by Penn Central to the hotels for 1966 is assumed to be at level shown of record for 1967.

[2]In partial reimbursement to Penn Central for payment in 1967 to prior lessee for the early cancellation of the lease.

Hotel income in 1967 nearly reached the level of 1960, but only after large capital expenditures relating to the Waldorf and a program that is only now beginning for the other hotels. From 1960 to 1964 the Waldorf invested over $5 million in capital improvements. A capital improvement program got under way at the Roosevelt in 1965, at the Barclay in 1966, and at the Commodore in 1967. Large-scale capital expenditures at each of these hotels continue.[14]

Both Penn Central and the NH creditors presented extensive evidence on the nature and scope of future capital expenditures. The witnesses on both sides represented highly qualified firms. In 1967 the five hotels expended over $2.2 million in capital. The witnesses for the creditors estimated that average future replacements would continue at a level of $2.3 million, and in addition two hotels would increase past levels of maintenance by $259,000.[15] The Penn Central witnesses estimated that the future capital expenditures of four of the hotels should be $3.4 million; if we add the creditors' Waldorf estimate, then Penn Central in effect argues that annual capital expenditures will exceed $3.8 million for all five hotels.

The evidence does not convince us that we should depart from the average 1964–1967 hotel income, except for the adjustment

[14]Hotel "capital expenditures" include such diverse items as china, linen, silverware, furniture, fixtures, carpets, as well as items connected with the structure.

[15]The creditors project extraordinary repairs of about $133,000 for the Commodore beyond the average past level of about $267,000; and $126,000 for the Barclay beyond the average past level of about $274,000.

for accrued and unpaid income. The Penn Central witnesses assumed they could project capital expenditures without relation to the room rates or occupancy rates needed to support such expenditures. Consequently, Penn Central presented no evidence regarding the future room rates or occupancy rates of the five hotels. Its witnesses spoke in very general terms about keeping the hotels "competitive," but on cross-examination showed they had in mind no specific competition nor any particular level of income the hotels should attain. Penn Central has not shown that the level of improvement implied by annual expenditures of $3.8 million is one that these hotels must attain in the ordinary course. One Penn Central witness suggested that the improvement program would recapture lost convention business; the testimony on its face implies that the program must have a beneficial effect on income.[16] Without the effect on income, we are unable to appraise the program.

We are unconvinced by the creditors' evidence for a different reason. At first the creditors presented evidence before the special master of only the increased revenues that the hotels should likely earn in the future. The future hotel income was represented to be $11.9 million per year. The study was made without relation to the capital expenditures that were admittedly necessary to attain that income. Later the creditors' same witness presented estimates of capital expenditures and the following rental estimates after replacements:

Hotel (1)	Profit Per Room After Replacements (2)	Rooms (3)	Totals (col. 2 x col. 3)
			Thousands
Waldorf	$1,516	1,798	$2,726
Commodore	826	1,847	1,526
Biltmore	1,805	909	1,641
Barclay	2,825	790	2,232
Roosevelt	1,388	1,070	1,485
Total			9,610

This increase of about $2,509,000 over average 1964–1967 hotel income is not supported. The witness' hasty estimate of capital expenditures was made without inspection of any one of the hotels or discussion with any management personnel; he relied on the annual reports from the hotels, national averages, and his general knowledge of the hotels. His earlier income study for the hotels was admittedly made without any capital expenditure figures.

[16] In several respects Penn Central's evidence resembled their earlier showing, which we rejected, regarding deferred maintenance on the New Haven. See 331 I.C.C. at 696.

Both sides agree that substantial capital expenditures must continue in the future. Neither side presents convincing evidence of what they will be, and hence do not add to what we already know from the experienced figures. The experienced figures suggest that the hotel income in those years supported the capital expenditures of those years. We assume that future increases in such expenditures will be tied to appropriate income estimates or they will not be undertaken. For present purposes, therefore, we will rely on average hotel income for 1964–1967 after capital expenditures and before the Waldorf repayment as indicative of the future hotel income, modified only by the accrued and unpaid hotel income of record.

Unpaid excess income.—The three-judge court concluded that NH could properly lay claim to a "sum to reflect NH's interest in surplus income accrued in 1964, 1965, and 1966." It stated that the value of this claim "would be around $3 million." NH can validly claim the following amount (on a 50-percent basis):

For 1964	$969,888
1965	472,243
1966	328,139
Total	$1,770,270

The trustees' liquidation study included $1,321,300 of this excess income item which the creditors concede must be deducted from the amount claimed for 1964–1966. The net claim to which NH is entitled in our computations is $448,970 for the 3 years.

The creditors argue that we should add to the Grand Central valuation the value of this claim through the date of inclusion. Manufacturers asserts that the reorganization court "said" that this credit should be made up to that date. Penn Central states that the court's opinion "suggests" this result. We do not read the opinion of the reorganization court to mean either a statement or a suggestion that the claim be paid through 1968. The court merely stated that we should "consider" the period 1964 to date when deciding upon NH's 50-percent interest in excess income. The discussion was not directed to the past claims, and we have complied with the court's suggestion that we consider the past period.

If we added NH's claims for 1967 and 1968 to liquidation value, we would be giving it a double value, once as a dollar claim and secondly in the capitalized value of its claim as of December 31, 1966. The bondholders' argument in effect seeks to move the valuation date forward; if we added NH's claims to excess income for 1967 and 1968 to the value of the estate, we would also have to make other adjustments, such as depreciation for 1967 and 1968;

and such re-evaluation of the estate might be quite different from the ultimate liquidation figure we have found.

The valuation date in this proceeding continues to be December 31, 1966. Any NH claim postdating the valuation date is included in the forecast of earnings and is settled by the value placed upon its interest as of December 31, 1966.

Summary.– Our liquidation valuation of NH's 50-percent interest in the excess income of the Grand Central Terminal properties is $28,887,000. A recapitulation of our findings in tabular form follows:

Line No.		Thousands		
	Income and revenue			
1	Terminal revenue (1964-1967 average)		$4,222	
	Office building income:			
2	1967 income	$5,644		
3	Increases	109		
4	Tower building	1,280		
5	Subtotal		7,033	
6	Hotel income		7,101	
7	Other income (1964-1967 average)		44	
8				$18,400
	Expenses			
9	Terminal expenses			18,850
10	Terminal profit			4,550
	Valuation of NH share			
11	NH share (50 percent basis)			2,275
12	Share capitalized at 8 percent[1]			28,438
13	Plus unpaid excess income			449
14	Grand Central valuation			28,887

[1] Unlike the three-judge court, we do not deduct the capitalized value of NH's guaranteed minimum payment of $160,000 to the Terminal Account, since we agree with the bondholders that the minimum should not enter into a capitalization of income after payment of all expenses.

Discount of the expenses of liquidation.–In the *inclusion* report, we assumed that the period of liquidation would be not less than 6 years, and consequently discounted the liquidation receipts to present value using a factor of 6 percent per year. The total discount was about $17.6 million (331 I.C.C. at 661). We did not discount the future expenses. The three-judge court held that, "if future receipts are to be discounted to present value, as they properly should, future expenses must likewise be"; and the reorganization court agreed. Upon reconsideration, we concur.

The parties are very close on the amount of the discount of liquidation expenses.[17] The Penn Central witness estimated the discount at $5,684,000 and a witness for the creditors estimated it at $5,669,000 which he changed to $5,724,000 on cross-examination. Both witnesses included real estate taxes of $16.2 million as a liquidation expense. In view of what we say hereinafter, liquidation expenses should exclude these taxes. If we exclude these taxes, Penn Central and the creditors would show the following discounts:

Discounted liquidation expenses net of real estate taxes

Year	Expense Estimates		Discount Factor	Discount	
	PC (1)	Creditors (2)	(3)	PC (col. 1 x col. 3)	Creditors (col. 2 x col. 3)
	Thousands			*Thousands*	
1	$10,453	$10,377	.02913	$304	$302
2	8,809	8,815	.08486	748	748
3	6,823	6,817	.13739	937	937
4	3,028	3,030	.18691	566	566
5	1,657	1,689	.23358	387	395
6	3,104	3,148	.27758	862	874
Total				3,804	3,822

We will, therefore, use $3.8 million as the appropriate discount of liquidation expenses excluding real estate taxes.

Accrued real estate taxes.—In the *inclusion* report we deducted from liquidation value the sum of $16.2 million, representing accrued and unpaid real estate taxes, as a liquidation expense. However, we also approved the contract between the trustees and Penn Central under which the properties would be transferred to Penn Central free and clear of liens. The three-judge court and the reorganization court concurred in holding that we had improperly duplicated the expense; the prior method "resulted either in an overstatement of the consideration to be received by the estate or an understatement of liquidation value."

We think that the proper treatment of this item is to remove it from the liquidation expenses. Under the agreement the liability will remain with the estate and not be transferred with the assets to Penn Central. It, therefore, should not be reflected as an expense attached to the prospective sale of the assets.

Penn Central argues that the full $16.2 million should not be shown as an increase in the liquidation value of the estate for two

[17] It is unnecessary to consider the differences between the parties' discounts of the proceeds, since we see no error in our prior opinion on this point.

reasons, first because they will be paid for by notes rather than cash, and secondly because a portion of the taxes will be forgiven. Chase argues that the settlement of liens by the estate "can be no proper concern whatsoever of Penn Central. *** If the New Haven's liability on any such claims is reduced, it is the NH and not Penn Central which must be the beneficiary." Under its view of the law, liquidation value must include the full amount of the tax claims and the estate is to reap the admitted windfall resulting from a settlement of the claim. We fail to see the fairness or equity of the result that Chase would reach, and decline to follow its suggestion.

The record shows that the market will discount the notes to be issued by the estate in payment of the full amount of these taxes by 10 to 12 percent. Just as it would be the cheaper way out for Penn Central to pay the purchase price adjustments in bonds, rather than cash, it is similarly cheaper for the estate to pay these taxes in notes rather than cash. A reduction of the taxes by 10 percent leaves an increase in liquidation value of $14.6 million. On the other hand, the record is barren of any evidence that the trustees will be able to compromise any of these claims; we will not reduce them further for the mere possibility of such a reduction.

Harlem River and Oak Point yards.–In the *inclusion* report we considered appraisals of the Harlem River and Oak Point yards submitted by Penn Central ($15,585,000), the creditors ($32 million for residential use and $26 million for industrial use) and by the trustees ($22,650,000, including land $18,440,000 and improvements $4,210,000 as of June 15, 1965; and $18,090,990, including land $15,959,000 and improvements $2,130,000 as of December 31, 1965). We rejected Penn Central's appraisal because its forced-sale concept did not reflect the probability that sale of any of the properties could be withheld for the most advantageous price. We found the creditors' $32 million appraisal to be speculative, and the three-judge court agreed, because a zoning change would be required before the properties could be devoted to the residential use upon which the appraisal was based. We found the $18,090,000 appraisal submitted by the trustees to be the most accurate and accepted that figure as representing the value of the yards in the event NH were liquidated and its line of railroad dismantled.

The reorganization court found sufficient support in the record for the appraisal we accepted. However, the three-judge court found "no adequate explanation in the Report for the rejection of the higher of the two estimates submitted *** for the New

Haven trustees, or, for that matter *** /the creditors'/ *** industrial use appraisal of $26 million, which in its main discussion of the yards the Commission does not mention." The three-judge court also requested that we clarify the question of whether reductions for liquidation expenses and discounts giving effect to the fact that it would take from 1 to 3 years to dispose of the yards were reflected in the $18,090,000 value we found for the yards as of December 31, 1965, and whether such reductions and discounts, if any, duplicated those made in our overall calculations of value for NH's property.

We rejected the creditors' $26 million appraisal without discussion because it was admittedly hastily prepared after only a cursory inspection of the improvements included in the yards and reflected an estimate of going concern value instead of liquidation value. The creditors' appraiser indicated that the trustees' appraisal was made by "an extremely well-qualified, thoroughly competent man who I know had done a complete job," and that "If I had viewed /the yards property/ as he /the trustees' appraiser/ viewed it, I might have come to his conclusion." There is nothing in the record, including the record compiled at further hearing following remand of the proceeding, which would warrant our accepting the creditors' $26 million estimate in preference to the trustees' estimate.

The three-judge court is correct in its understanding that the trustees' appraisal of June 15, 1965, was based on an assumption that the properties involved were to be continued in use as railroad yards. This point was clarified at the further hearing in the testimony that the $22.7 million appraisal of the yards was made on the basis that they were operating railroad properties with facilities for shippers and tenants to be served by railroad. This appraisal was confined to the properties embraced within the physical limits of the two yards.

The further hearing following remand also confirmed the fact that the $18.1 million appraisal we accepted was based on the assumptions that NH's railroad had ceased to exist, its tracks were removed from the yards, power was shut off leaving the yards without electricity and power, and the properties had become industrial facilities without any railroad service. No consideration was given in this appraisal to the interchange connection with Penn Central's Port Morris branch via trackage extending from the Oak Point yard.

An example of the difference in approach in the trustees' two appraisals is afforded by the so-called REA Building in the Harlem River yard. This building was specially built for REA Express with four tracks running through the center of its ground floor. In the first, and higher, trustee appraisal the building was valued at $675,000 because of these tracks and the railroad service they provided. In the second, and lower appraisal, it was assumed that the tracks were dismantled. This would require reconstruction of the ground floor. The building would then be suitable only for an entirely different type of tenant. Without tracks, it would have a lower rental value. Its appraised value was, therefore, reduced to $400,000 in the second appraisal. Differences in the values of various other tenant-occupied buildings in the two yards resulted from following similar procedures in their appraisals.[18]

As previously indicated, in disposing of the question of the value of the Harlem River and Oak Point yards in the *inclusion* report, we assumed that NH's railroad system on liquidation would be entirely dismantled, including the approximately 2 miles of main-line tracks connecting the two yards, which are not immediately adjacent. The liquidation value we assigned the yards reflected that assumption. No other method of liquidation was considered, or remanded to us for consideration by the courts, or previously raised before us by the parties. However, through cross-examination and testimony at the further hearing following remand, the creditors have raised the question whether it should always be assumed that in the event NH is liquidated, its tracks would be removed from the yards and its buildings and land sold as nonrailroad-served real estate, or whether it should be assumed that upon liquidation, the two yards would be sold, as is, to another railroad for continued operation.

The creditors contend that in the event of NH's liquidation, Penn Central would not wish to lose the traffic and revenues generated by shippers and receivers served by the yards, particularly the newly established Hunts Point Wholesale Market, the largest receiver, but not originator, of rail traffic in the area. The market is located north of, but not adjacent to, the Oak Point

[18] There are also several small, old, wood, metal or brick buildings in the yards devoted solely to railroad use. They were assigned a value in the first, or operating railroad, appraisal. In the second appraisal, they were assumed to serve no purpose if NH's railroad were to be dismantled. Accordingly, they were assigned no value at all in the second appraisal.

yard. They contend that there is presently at Oak Point, from which the market is served by NH, a substantial interchange between Penn Central and NH of cars (2,328 during August 1968) moving via through Penn Central trains from the latter's Alfred E. Perlman yards at Selkirk, N. Y., to Penn Central's Westchester yards and then by local switching to Penn Central's Port Morris branch for interchange at Oak Point.[19] The creditors point to plans now under way to expand the Hunts Point Market by including citrus fruits and meat, with eventual wholesale markets for butter, eggs, fish, and flowers. The rail traffic into the market is mostly shipped out again by motor truck. The creditors assert that even if Penn Central does not purchase the yards for continued operation in the event of NH's liquidation, the yards would be purchased by some other railroad.

In addition to the routes via NH's main line into the Harlem River and Oak Point yards area and the Penn Central's Port Morris branch line, there is also a route over the line of New York Connecting Railroad[20] via the Hell Gate bridge and a track connection to Bay Ridge, Brooklyn to which cars are now floated from the New Jersey pierheads of The Central Railroad Company of New Jersey (CNJ), The Baltimore & Ohio Railroad Company, Penn Central and the Lehigh Valley Railroad Company. The creditors also allege a third means of providing a service, namely, car floats to Oak Point yard float bridges which were formerly operated by NH but abandoned several years ago. The creditors admit that the car float bridges would require rehabilitation but argue that thereafter they would provide a practical access to the Oak Point-Harlem River yards area by any of the present carriers now serving the area.

It is extremely doubtful that railroad service would continue to the Harlem River and Oak Point yards if NH's system were liquidated. The creditors contend that Penn Central would be legally obligated, as part of its line haul, to spot cars at Hunts Point and at industries in the Oak Point and Harlem River yards if NH were liquidated, even if this involved plant switching beyond

[19]The interchange connection consists of a single track in an underpass under NH's main line into Oak Point. Traffic movement at the interchange is primarily from Penn Central to NH. Interchange cars arrive at Oak Point unclassified and are classified at that point by NH. Cars destined to Harlem River are moved over NH's main line from Oak Point in the reverse direction from the direction they are received from Penn Central. A direct movement from Penn Central's Port Morris branch to the Harlem River yard is not possible.

[20]Owned jointly by NH and Penn Central on a 50-50 basis.

Penn Central's present boundary. However, Penn Central disputes this contention, pointing out that the market and yards' industries are local to NH's line and are not presently stations on Penn Central. The latter argues with considerable logic that it would not be legally obligated to perform switching service beyond its own line or extend its line to serve NH's industries if the present joint rates were terminated by NH's liquidation.

Penn Central testified that the preponderance of the present traffic in the area of the yards is in perishable commodities destined to Hunts Point which it finds unprofitable, and that of the 2,328 cars interchanged with NH at Oak Point during August 1968, only 415 cars or an average of 13.3 daily were destined to industries in the two yards. Penn Cental declares that in the absence of NH's line, it would not be interested in serving Hunts Point because, aside from the unprofitability of the perishable traffic, it would lack the necessary track clearances and the yard facilities to classify the cars destined to the market. Penn Central's testimony concerning the unprofitability of perishable traffic is supported by the reports made periodically to the Commission by all railroads serving this territory in connection with our rail burden studies. Year after year these reports indicate that this traffic is handled at a loss; our most recent data on the principal traffic of this type, destined for the East, is set forth on the following page.[21]

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[21] Computed from "Procedures for Developing Rail Revenue Contribution by Commodity and Territory, Year 1965," statement No. 1-68, issued as information by the Commission's Bureau of Accounts; and see *Port of New York Authority v. Aberdeen & R.R. Co.*, 321 I.C.C. 738, 742-43 (1964).

Relationship of revenue to cost of predominant movements of certain perishable traffic destined for official territory, year 1965

Line No.	Item	Commodity 012, fresh fruits and tree nuts			Commodity 013, fresh vegetables		
		Box cars	Refrigerator cars		Box cars	Refrigerator cars	
		Official territory to official territory	South to official territory	West to official territory	Official territory to official territory	South to official territory	West to official territory
1	Carload costs[1]	$11,657	$5,896	$30,235	$4,254	$7,947	$46,561
2	Ton costs[1]	169	80	606	80	93	913
3	Ton-mile, way train[1]	630	372	1,952	297	431	2,943
4	Ton-mile, through train[1]	2,396	4,679	56,332	1,362	6,689	76,067
5	Car-mile, way train[1]	1,268	2,338	10,518	463	3,151	16,197
6	Car-mile, through train[1]	7,379	40,245	439,896	3,055	67,928	608,308
7	Loss and damage[2]	4,849	2,454	9,948	1,905	2,371	12,484
8	Out-of-pocket cost–Total	28,348	56,064	549,487	11,416	88,610	763,473
9	Constant cost, terminal[3]	1,716	773	3,918	810	898	5,906
10	Constant cost, line haul[3]	2,618	5,167	59,804	1,458	7,326	80,922
11	Fully distributed cost–Total	32,682	62,004	613,209	13,684	96,834	850,301
12	Revenue statement No. 1-68, table 8	23,566	52,310	377,676	12,342	63,330	542,768
13	Percent: revenue to out-of-pocket cost L. 12÷L. 8	83%	93%	69%	108%	71%	71%
14	Percent: revenue to fully distributed cost L. 12÷L. 11	72%	84%	62%	90%	65%	64%

Notes: All references are to statement No. 1-68:

[1]Multiply the work units for each traffic shown on table 8, pages 28 and 29, by the corresponding unit costs on table 1, pages 14 and 15. Short-line ton-miles and car-miles were separated between way and through trains by the method illustrated on page 6.

[2]Loss and damage claim payments per ton on table 7 times the number of tons on table 8. L&D per ton for commodity 012 is the average, weighted for volume, of lines 2 and 3, table 7.

[3]The numbers of tons and ton-miles on table 8 times the corresponding unit costs on table 6.

The record does not support any finding of substantial need for Penn Central service that would justify the construction by that carrier of the trackage necessary to connect Harlem River and Oak Point yards and the latter yard and Hunts Point, if NH were to be liquidated. Nor is there any evidence that the expenditures necessary to correct clearance deficiencies on the Port Morris branch would be warranted by the revenues resulting therefrom. On this record, and the assumption of NH's liquidation and the dismantling of its system, Penn Central would not serve, and could not be compelled to serve, the Harlem River or Oak Point industries, or the Hunts Point Market.

It also seems unlikely that rail service by a carrier other than Penn Central would be performed in the yards if NH were liquidated. The weak financial structure of the New York Connecting Railroad, to which we referred in the *inclusion* report (331 I.C.C. at page 678), together with the nonproductive character of the traffic, would appear to preclude that carrier from making the investment necessary to acquire NH's yards and their appurtenant facilities, even if Penn Central's interest in the company did not prevent its doing so. The creditors admit that service to the yards via the abandoned car float bridges is probably the least desirable approach to the problem and offer no estimates of the costs of rehabilitating the bridges or the revenues which would be derived from the operation. Neither have they made any determination of the profitability of the yard traffic to harbor carriers or whether any of the harbor carriers are interested in the traffic. There is nothing in the record to establish that any existing terminal carrier is interested in acquiring the NH yards, that any serious consideration is being given to the formation of a new terminal carrier to do so, or that the city of New York is interested itself in acquiring the yards for continued railroad operation.

Accordingly, we find that the $18,090,000 appraisal of the trustees which we accepted in the *inclusion* report was based correctly upon an assumption that all railroad service to the Harlem River and Oak Point yards would terminate upon the liquidation of NH.

Finally, our valuation did not duplicate any of the expense deductions. Our $18 million appraisal of these yards was derived from an appraisal of NH's Harlem River branch of which they form a part. The entire property in the branch, including the two yards, was appraised at $24,577,279 (rounded off by the

appraiser to $24,600,000). Of this total amount, the Harlem River yard accounts for $10,319,900 (land $9,189,900, improvements $1,130,000) and the Oak Point yard for $7,771,090 (land $6,771,090, improvements $1 million).

From the rounded-off total value of the Harlem River branch, $24,600,000, the trustees' appraiser deducted $3,929,330 (consisting of real estate taxes $2,167,300, brokerage commissions $1,225,700, real estate department expenses $500,000, appraisal fees $25,000 and transfer taxes $11,330) to arrive at an estimate of net liquidation value for the whole Harlem River branch of $20,670,670.

The appraiser's net liquidation figure was not carried over, however, into the overall calculation of the liquidation value of NH's property. Instead, his gross figure of $24,577,279 was carried over. The $107,412,000 we found in the *inclusion* report to be the gross value of NH's land includes the gross value of the land in the Harlem River and Oak Point yards. The gross value of the buildings in the two yards was similarly carried over, unreduced for liquidation expenses, into the overall valuation of their appropriate property classes. Since deductions for liquidation expenses were made only from the overall valuation in the *inclusion* report, there were no duplications of deductions involved; and there is no necessity for modifying our previous finding as to the value of these yards.

Deduction for depreciation to adjust valuation results to December 31, 1966.—In finding the liquidation value of NH's assets as of December 31, 1966, in our *inclusion* report we deducted $3 million for 1966 depreciation, but failed to set forth particulars. See 331 ICC 695.[22] The three-judge court concluded that "this item is not found in the report and its derivation is obscure." Penn Central has presented data in this reopened proceeding purporting to show that the amount for depreciation in the year 1966 is $3.7 million.[23] As adjusted, its figure becomes $3.2 million, as set forth below:

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[22]The depreciation item of $3 million is referred to in the Government's joint brief before the three-judge court.

[23]Penn Central's exhibits also include equipment and other property sold or otherwise disposed of during the year 1966. However, such transactions are to be given effect in the purchase price adjustments pursuant to section 9 of the purchase agreement and will not be duplicated in the present deduction for depreciation for 1966.

	Penn Central exhibits	As adjusted
Locomotives	$533,726	$533,726
Freight cars	1,033,719	688,729
Passenger cars	1,144,800	1,144,800
	2,712,245	2,367,255
Other property	981,570	866,570
Totals	3,693,715	3,233,825
Decrease		459,890

Depreciation of equipment for 1966 was calculated by Penn Central on an engineering basis by apportioning to that year an amount based on (a) the liquidation value as of December 31, 1965, less the estimated scrap value, and (b) the estimated remaining service life. This is a fair and reasonable procedure and we find the basic data correct, except for the data on the service lives for several classes of freight cars. We have restated the figures for the remaining useful life of the cars, using a remaining life based on a full-time service life of 25 years from date of construction of the cars to the end of their useful life and sale as scrap. A full-time useful life of less than 25 years used in Penn Central's calculation is too short for freight cars. The adjusted amount for depreciation of the freight cars for 1965 is $688,729. See appendix 1 hereto.

Penn Central's depreciation study assumes, consistent with the trustees' liquidation study, that upon liquidation the trustees would disaffirm whatever obligations on equipment exceeded the sale value of such equipment. This has the effect here of removing $8.7 million of equipment values from the depreciation base. We concur in the approach for the purpose of computing a depreciation figure for 1966, since we have not undertaken a re-evaluation of the estate. However, this approach for purposes of depreciation and valuation of the NH assets does not foreclose us from estimating a lesser cost to Penn Central of assuming NH's equipment obligations than in the *inclusion* report; and we later adjust that figure.

Depreciation of property, other than equipment, for 1966 was calculated by Penn Central for structures under a procedure similar to that described above for equipment; for railroad ties on an estimated useful life of 40 years; and for ballast at an annual replacement rate of 25 percent on the grounds that stone ballast becomes clogged with dirt and foreign substances and if not cleaned every other year will lose 25 percent of value. We find the procedure used for calculating the depreciation of the property to be fair and reasonable and the amounts to be correct,

except the amount for depreciation of ballast. Penn Central's application of a 25 percent loss of value for 1966 amounts to $275,000. However, expenditures for maintenance of ballast amounting to $160,000 were incurred during the year, thus restoring value in that amount in the ballast sections. Accordingly, we will reduce the allowance for depreciation of ballast by $160,000 and approve deduction in the amount of $115,000 for 1966. On this basis the correct amount of total depreciation for property, other than equipment, for 1966 is a reduction from $981,570 to $866,570.

Manufacturers contends that for railroad ties, a proper useful service life is 50 years, rather than the 40 years as used by Penn Central. Manufacturers cites our *Norfolk and Western* merger decision[24] as ruling that treated ties have a useful life of at least 50 years. Our statements regarding tie lives in that proceeding simply appraised the evidence presented by certain railroads involved in the merger, which had used varying useful lives. We rejected their cost estimates for maintenance of ties and other track property to normalize annual earnings for purposes of the particular proceeding. The useful life of railroad ties in this reopened proceeding is 40 years, based on the evidence herein; and a depreciation rate of 2 1/2 percent with resulting depreciation for 1966 amounting to $284,000 accordingly is justified. In any event, a 50-year tie life would reduce the depreciation by less than $60,000 and would not change the result herein, namely that we adhere to our prior estimate of $3 million as an appropriate and reasonable depreciation estimate for 1966.

NH's investment in B&P.—The three-judge court questioned our acceptance in the *inclusion* report of the trustees' investment in stock and debentures of the Boston and Providence Railroad Corporation at book value, or $4.7 million. The creditors value the property at $11.2 million which is the trustees' estimated liquidation value of the B&P properties before deducting liquidation expenses of $3.1 million. According to the three-judge court, the net liquidation value of B&P, $8.1 million ($11.2 million gross value less $3.1 million liquidation expense) should be reduced by $2.3 million, which amount NH is obliged to pay under B&P's reorganization plan for the B&P stock.[25]

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[24] *Norfolk & W. Ry. Co. and New York, C. & S. L. R. Co.-Merger*, 330 I.C.C. 780 (1967).

[25] NH will acquire the entire B&P stock for $110 per share and become the sole stockholder of the B&P. See *Boston & P. R. Corp. Reorganization*, 327 I.C.C. 10, 13-14 (1966).

As the three-judge court points out, at the time we approved the B&P plan of reorganization, it appeared that some parts of the B&P line might be acquired by a public agency for continued railroad operation or as a highway route, at prices substantially in excess of their appraised value. To permit B&P shareholders to participate in any windfall of this kind despite the acquisition of the publicly held stock as required by the B&P reorganization plan, we authorized issuance of certificates of contingent beneficial interest (CCBI's) in the proceeds of any such transaction involving more than $500,000 which occurs prior to December 31, 1978.[26] Former shareholders of B&P are entitled to 52 percent of these CCBI's and NH the remaining 48 percent.

We found in the *inclusion* report that there was no firm basis for assigning any value to these CCBI's. The creditors at the further hearing following remand renewed their contentions that the CCBI's have a definite value which should be credited to NH when its properties are acquired by Penn Central.

According to the creditors, the current market value of B&P stock is between $210 and $230 per share. The $100 to $120 difference between the market value of the stock and the $110 per share NH is required to pay for the outstanding shares in the hands of the public is asserted by the creditors to represent the present market value of the CCBI's. The value assigned by the creditors to the 48 percent of the CCBI's acquired by NH and then by Penn Central would thus lie between $1.9 million and $2.3 million, with the midpoint, $2.1 million, being advanced by the Committee as the value that should be recognized.

The market value of the few shares of B&P stock traded in the past few months was undoubtedly influenced by numerous factors other than the actual equity in B&P which they represent, including the activities of speculators. In our opinion the market price of the B&P shares does not necessarily reflect either the real or potential value of such shares or the CCBI's to be issued therefor.

In reviewing the basis for evaluating NH's interest in the B&P, we find that NH has itself provided data that afford a basis for determining a reasonable value for the CCBI's.

NH held about $5 million of B&P debentures when we approved the B&P reorganization plan. Its stockholdings of about 20,000 shares of B&P[27] must have been worth the same $2.3 million

[26] *Boston & P. R. Corp. Reorganization*, supra, 14-17.

[27] There are 15,918 shares registered in NH's name. In addition, NH would receive under the reorganization plan the 3,272 shares in the B&P debenture sinking fund and 40 B&P treasury shares.

that NH was willing to pay the public holders for their 20,000 shares. Accordingly, NH valued its security interest in the B&P at $7.3 million. As noted earlier, the three-judge court would value NH's interest in the B&P assets on liquidation at $5.8 million after payment to the public holders for their interest.[28] When it agreed to the B&P reorganization plan, NH must have been placing a value of $1.5 million on its CCBI holdings in order to reconcile the valuation it placed on its interest in the B&P assets with the valuation it placed on its interest in B&P securities.

The conclusion that the CCBI's have substantial value is supported by the negotiations conducted by NH and the Federal Government during the *B&P Reorganization* proceeding. We then found that substantial concessions made by the Government justified a pledge of the CCBI's to the retirement of the new B&P bonds. We further found that the issuance of the CCBI's to NH was obviously a factor in the Government's decision to accept an amount less than that to which it was entitled. (327 I.C.C. at 16).

In the *inclusion* report, therefore, we undervalued the NH's interest in the B&P in two respects. First, NH's interest in the B&P assets which we valued at $4.7 million should be valued at $5.8 million (the difference between the liquidation value of the B&P assets and the amount NH had agreed to pay the public holders for their interest in those assets). Second, NH's interest in the CCBI's to which we gave no value, should be valued at $1.5 million under the analysis set forth above. Accordingly, we conclude that NH's interest in the B&P totals $7.3 million.

This valuation of NH's interest in B&P is based upon the requirement we herein make that Penn Central assume NH's obligation to the public holders and become the sole owner of the B&P.

Summary.—The gross value of the NH assets under the trustees' study, which we adopted in the *inclusion* report, was $230.3 million of which $32.4 million would be retained by NH. The net liquidation value under the prior findings was $125.8 million. The following table recapitulates the prior report and the findings herein on the liquidation value of the NH assets:

[28] We found the liquidation value of B&P to be $8.1 million. NH agreed to pay the public holders $2.3 million for their interest, leaving $5.8 million as NH's interest.

		Millions
Gross value of assets[1]		$232.9
Less assets retained or covered by closing adjustments		32.4
		200.5
Less liquidation expenses:		
Six-year liquidation excluding accrued taxes and interest thereon[2]	$43.7	
Discount to present worth	3.8	39.9
		160.6
Less discount of proceeds to present worth		$17.6
		143.0
Other downward adjustments[3]		6.2
		136.8
Less 1966 depreciation		3.0
		133.8
Plus Grand Central Terminal properties		28.9
Net liquidation value		162.7

[1] Includes an upward adjustment of $2.6 million for NH's interest in B&P.

[2] In the *inclusion* report we found that liquidation expenses would total $59.5 million, and we here exclude $14.6 million of accrued real estate taxes, and $1.2 million of interest thereon. For latter item, see 331 I.C.C. at 663.

[3] See 331 I.C.C. 668-677.

The net liquidation value of the NH estate is $162.7 million. A property value of this sort inheres in the assets if we assume that the railroad may immediately shut down and begin a 6-year program of selling off the road parcel-by-parcel, and virtually tie-by-tie. It is the valuation we used in the *inclusion* report to appraise the fairness of the purchase agreement price then available for use. It is now the valuation that the creditors argue they, or the estate, are entitled to as a matter of constitutional law. We next turn to whether the estate is entitled to the foregoing net liquidation value as a matter of law, or whether there are other considerations on this record that should enter into the fixing of a fair price for the NH assets.

OTHER PRICING CONSIDERATIONS

The three-judge court and the reorganization court have suggested that the Constitution requires us to establish a price for the assets of the estate at no less than their liquidation value. They reason that since the creditors have an absolute right to bring about the abandonment of the deficit-ridden railroad, they have the further right to obtain the values that sales of the railroad in parcels for their highest and best use would bring. In the *inclusion* report we did not address ourselves specifically to

the minimum price to which the estate was entitled. The law here is not settled and the question in many ways is novel. The courts accordingly permitted us to consider alternative pricing theories prior to the final resolution of the question by the Supreme Court.

Valuation at best is inherently imprecise, involving broad areas of judgment. This is especially so in the case of a bankrupt railroad having no prospect of future income as it is presently operated. It appears, therefore, that an inflexible rule of law prescribing liquidation value (as computed above) as the minimum to which the creditors are entitled might lead to unfair results. In regard to this we believe there are other considerations relevant to the price the creditors should expect to receive and Penn Central to pay. We proceed further in this analysis, because we believe that the liquidation value we have found above is not itself a fair and equitable price and is not required as a matter of law. It is fair neither to the estate nor to Penn Central. We, therefore, believe it is necessary and proper to consider other values in reaching our final price.

In the *inclusion* report, we found that the consideration Penn Central had agreed to pay would equal liquidation value there shown, and that made it unnecessary for us to explore other pricing considerations. The liquidation value that results in this reopened proceeding exceeds the agreed price, obliging us to make a new determination as to whether the price resulting from such a valuation is fair.

The establishment of liquidation value as a pricing floor on this record must assume that the NH may be shut down at once and be liquidated in parcels. Such a pricing theory assumes that the public may be denied an opportunity to be heard. It is wholly inconsistent with the requirement we have imposed on Penn Central to absorb the NH, which requirement rests entirely upon the public's need for a continuing NH. Any assumption that NH may be shut down and broken up must necessarily permit the conclusion that Penn Central may be relieved of its inclusion obligation. It is inequitable to conceive at the same time both a right in the bondholders to break up the NH and an obligation on Penn Central to keep it going. The demands of equity are no more satisfied by conceiving that the bondholders have a constitutional right to shut down the NH which is superior to the public's right to keep it going.

The foregoing liquidation value assumes that this Commission has no function under the Interstate Commerce Act to decide whether public convenience and necessity permit the abandonment

of NH's entire line or portions of it. In view of our often repeated findings that there is a public need for the services of this railroad, there is no warrant for assuming that the creditors may now break up the railroad or devote the properties to another use. The estate is not relieved of its obligation to serve the public. A price that is premised on outright rejection of that obligation is inequitable and awards the estate a windfall that is not supported by any record evidence.

Where foreseeable earnings of a railroad are not negative, but merely inadequate, its liquidation value may exceed the capitalization of those earnings. It is unlikely we would consider the abandonment of the railroad in those circumstances or the liquidation value of its assets. But just as we cannot conclusively presume that the public interest would require the continuation of a marginal railroad, we cannot conclusively presume that the public interest would allow the dismantling of a carrier which is losing money. This much is clear, however; section 77 of the Bankruptcy Act was intended in part to make continued operation possible through reorganization.

In relying on the liquidation value for the NH parcels, the three-judge court cited *Railroad Commission* v. *Eastern Texas R. R.*, 264 U.S. 79 (1924), which holds (at 85):

> The usual permissive charter of a railroad company does not give rise to any obligation on the part of the company to operate its road at a loss. No contract that it will do so can be elicited from the acceptance of the charter or from putting the road in operation. The company, although devoting its property to the use of the public, does not do so irrevocably or absolutely, but on condition that the public shall supply sufficient traffic on a reasonable rate basis to yield a fair return. And if at any time it develops with reasonable certainty that future operation must be at a loss, the company may discontinue operation and get what it can out of the property by dismantling the road. To compel it to go on at a loss or to give up the salvage value would be to take its property without the just compensation which is a part of due process of law. The controlling principle is the same that is applied in the many cases in which the constitutionality of a rate is held to depend upon whether it yields a fair return.

The *Eastern Texas* opinion cites in turn *Brooks-Scanlon Co.* v. *Railroad Commission of Louisiana*, 251 U.S. 396 (1920); and *Bullock* v. *Railroad Commission of Florida*, 254 U.S. 513 (1921).

In *Brooks-Scanlon*, the Supreme Court held that a railroad may abandon even a branch line that loses money, citing *Munn* v. *Illinois*, 94 U.S. 113, 126 (1876). The rationale of *Brooks-*

Scanlon and *Munn* v. *Illinois* was overruled *sub silentio* by the Supreme Court in *Colorado* v. *United States*, 271 U.S. 153, 166, 168 (1926), where the Commission's role in weighing the advantages and disadvantages of an abandonment of branch lines that lose money was preserved.

In *Bullock*, the Supreme Court confined the rule of *Brooks-Scanlon* to situations "apart from statute or express contract." The demands of the public interest pursuant to statute may limit the abandonment right.

The Supreme Court in our view has never flatly held that a deficit-ridden railroad has an absolute right to abandon, liquidate, and sell the parcels. The thrust of *Eastern Texas*, *Brooks-Scanlon*, and *Bullock* is that a deficit railroad has a right to stop the deficits.[29] It does not follow, we believe, that it has the immediate right to abandon, nor the rights derived therefrom to break up the railroad and to receive the maximum salvage value.[30]

The creditors' basic right is to a fair and equitable price. A fair and equitable price under section 5 of the Interstate Commerce Act as well as under section 77 of the Bankruptcy Act means a price that is fair both to the buyer and to the seller. The standards of the two sections are comparable; and we believe the Constitution prescribes no higher test.

There is some suggestion in the older abandonment cases that the right to abandon an unprofitable line was supported by the principle then governing the constitutionality of a rate. *E.g.*, see *Eastern Texas* opinion, *supra*. The principle there referred to was the protection of property rights and asset values it was then thought the Constitution guaranteed to a regulated utility under the rule of *Smyth* v. *Ames*, 169 U.S. 466 (1898). The Supreme Court ended its reliance on property valuation as the constitutionally prescribed test, however, in *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591, 602 (1944),

[29] The three-judge court cited these cases for "the constitutional right of NH to cease operation and liquidate." Later it merely referred to "their constitutional right not to be required to operate the property at a perpetual loss."

[30] See *In re Chicago, R. I. & Pac. Ry.*, 50 F. Supp. 535, 562-63 (N.D. Ill. 1943), affirmed 157 F. 2d 241, cert. denied 329 U.S. 750. All that was held in *New York Central R. Co. Acquisition of Boyne City, G & A. R.*, 180 I.C.C. 538 (1932), cited by the creditors, was that Central was required to pay the commercial value of the smaller line which was more than twice its scrap value. Under *New York Central Unification*, 150 I.C.C. 278, 322 (1929), the Commission had required Central to pay "commercial value" of the smaller carrier and rejected Central's offer of one dollar in the *Boyne City* case.

and held, "that the Commission was not bound to the use of any single formula or combination of formulae in determining rates." The Federal Power Act had required that commission to fix a "just and reasonable" rate, language comparable to the mandates of sections 5 and 77 to fix "just and reasonable," "equitable," or "fair and equitable" terms. The Supreme Court held "there are no constitutional requirements more exacting than the standards of the Act," and that "a rate order which conforms to the latter does not run afoul of the former" (at 607).

A similar suggestion was made by the Supreme Court in *Schwabacher* v. *United States*, 334 U.S. 182 (1948), where equity holders in a transaction under section 5 of the Interstate Commerce Act asserted a right to liquidation value under certain provisions of State law. The Supreme Court rejected the alleged State right, and held (at 201), that "any such rights are, as a matter of federal law, accorded recognition in the obligation of the Commission not to approve any plan which is not just and reasonable."

If a losing railroad has a right to abandon and to obtain proceeds equaling salvage value based on its right to a fair rate of return, it has a right after *Hope Natural Gas* only to such proceeds as are fair and reasonable. If before *Hope*, the agency was limited to preserving such asset values as the railroad might obtain upon abandonment and sale, then after *Hope* the agency might establish a fair price, assuming a buyer were available, without relation to the piece-by-piece liquidation values. However, it is unnecessary to explore this in depth in this report. The alleged right to liquidation values derives from an alleged right to abandon; and there are recognized limitations on the right to abandon that in themselves limit the creditors' entitlement to the liquidation value we have computed under the court's instructions. Under section 1(18) of the Interstate Commerce Act, the Commission is empowered to impose reasonable limitations on the abandonment right. The pricing out of such limitations permits us to reach what we consider to be a fair price on the present record, and we need go no further.[31]

[31] For example, we do not reach Penn Central's argument that we should consider the prices at which the present NH bondholders purchased their bonds over the past several years. Penn Central's evidence suggests there has been very active trading in the bonds and that the creditors purchased their bonds at substantial discounts from face value.

Limitation on the right to abandon.—The establishment of a price based on the immediate liquidation of the railroad assumes there can be an immediate abandonment. The act imposes on the carrier, however, a duty to request permission to abandon its lines. "A part of the capital dedicated to a railroad enterprise cannot withdraw itself without authorization any more than all of the capital can withdraw itself and abandon the railroad without approval." *Schwabacher* v. *United States*, 334 U.S. 182, 201 (1948). In *Meyers* v. *Jay Street Connecting Railroad*, 259 F. 2d 532, 536 (2d Cir. 1958), the Court of Appeals held that a mere showing of operating losses was not sufficient to "outweigh the strong purpose of the Interstate Commerce Act to prohibit the abandonment of railway service without the approval of the ICC." We must hear the communities that would be affected by the abandonment. If there is hope of a public takeover of segments, we must allow time for the States and communities to present their plans.

The three-judge court rejected Penn Central's reliance on the probability of "lengthy abandonment proceedings * * * during which large cash losses would be incurred and the property would further depreciate." The creditors argued in that court "that if inclusion of NH in Penn Central had not been in prospect, the NH Trustees would have been under a duty to initiate abandonment proceedings as soon as they reported, on December 31, 1963, that there was no prospect for independent operations of NH." That, of course, is hindsight observation and hardly a basis for determining price at this time. The fact is that both the creditors and the trustees exercised options,[32] assuming the risks involved therein, and the bondholders may not now be heard to ascribe to someone else the responsibility for the selection of their course of action, or inaction. The court stated that since "a considerable portion of the losses will be borne by the NH estate * * * there would be no justification for a double deduction." This rationale for rejecting Penn Central's argument is now weakened by our order today which requires inclusion by January 1, 1969, imposes all future losses after that date on Penn Central, and requires Penn Central to absorb more than half of the operating losses since consummation of its merger.

The court's further reasoning suggests that we cannot look back to what might have been in 1962 or 1963, and may now consider to what extent "lengthy abandonment proceedings" would

[32]The trustees' petition for inclusion in Penn Central was authorized by Order No. 109 of the reorganization court on June 19, 1962. The order was entered after notice and hearing and was unopposed.

reduce the value of the estate. The three-judge court correctly stated that if the trustees had presented abandonment applications as an alternative to a sale to Penn Central,

> the Commission would almost certainly have deferred their consideration for a reasonable period while inclusion was being explored.

We are only required in this proceeding to consider the alternatives that are now available to the creditors, not what might have been available in 1962 or 1963. As the three-judge court added, the creditors "by investing in a railroad * * * subject themselves to such interim losses as are reasonably incident to working out the solution most consistent with the public interest."

It would not be possible to conclude an abandonment proceeding in less than a year in a matter involving the complexity and size of the NH system. In Finance Docket No. 19861, *New York, Ontario and Western Railway Company, et al., Receivers Abandonment*, decided October 10, 1957, we authorized the abandonment of a system about one-third the size of the NH system 9 months after receivers were appointed and the reorganization proceeding concluded. In *Rutland Ry. Corp. Abandonment of Entire Line*, 317 I.C.C. 393 (1962), we permitted the abandonment of a line about one-fourth the size of the NH system in 10 months from the date of the application; and litigation continued for another 10 months. If the States or the Federal Government requested time to prepare studies, as we think they might, the time lapse between the filing of the application and the decision would approach 2 years.

We believe the potential costs of the abandonment route may properly be reflected in a reduction of the price Penn Central is to pay. Since the creditors derive a right to liquidation value from an alleged right to abandon, they cannot complain if we adjust the liquidation value of the estate by what they would be forced to bear if abandonment occurred.[33]

There are two aspects of this reduction in the price. First, the minimum 1-year delay before the start of liquidation means that the liquidation proceeds should be discounted to present worth by an additional $7,946,000. The figure is the difference in the dis-

[33] In *Market Street Railway v. Railroad Commission*, 324 U.S. 548 (1945), the Supreme Court held that a money-losing streetcar system was entitled to a return on whatever value it had not lost by operation of economic forces, whether it be its scrap value or some other amount. The present reductions reflect real economic loss that is potential and not hypothetical in any future abandonment of the NH.

count over 6 years and the discount over 7 years shown in the following table:[34]

Net receipts before taxes per creditors	Over 6 years		Over 7 years	
	Factor[1]	Discount (column 1 x column 2)	Factor[2]	Discount (column 1 x column 4)
Thousands		*Thousands*		*Thousands*
$74,424	.02913	$2,168	.08486	$6,316
42,013	.08486	3,565	.13739	5,772
21,172	.13739	2,909	.18691	3,957
7,805	.18691	1,459	.23358	1,823
134	.23358	31	.27758	37
4,171	.27758	1,158	.31905	1,331
Totals		11,290		19,236

[1]The factors used to reflect the total amount of the discount are the reciprocals of those used by the creditors and Penn Central to compute the net proceeds after discount.

[2]The reciprocals are also used here, except that it is assumed that a preliquidation period of 1 year ensues before the 6-year liquidation period begins.

Second, a 1-year delay before the start of liquidation would also mean that the estate would spend $4,940,000 in preservation costs, and experience an additional accrual of $2,500,000 of real estate taxes. A 1-year delay before the beginning of liquidation would bring a total diminution in the worth of the estate of at least $15,386,000.

Limitation on the right to break up the railroad.—There is a further limitation on the rights of the NH creditors which the price may lawfully reflect in the circumstances of the present case. The liquidation value urged by the creditors assumes not only the immediate right to abandon, discussed above, but also the right to break up the railroad and sell the parcels for their highest and best price. We think such a right may be restricted when a buyer for the entire bulk of the NH properties appears who will continue the operation of needed services.[35]

[34]We employ the creditors' schedule of the receipt of the liquidation proceeds in the table to compute the difference between a 6 and 7 year period. We do not rely upon the schedule to show the true discount to present worth over 6 years, since the creditors' schedule results in an understatement of the 6-year discount and a departure from the finding in the *inclusion* report that the discount would be $17,563,000.

[35]In many cases we have imposed the condition that the carrier shall sell segments of the line at not less than net salvage value to a prospective buyer for continued operation before dismantling the line. Failure to comply with the condition has resulted in cancellation of the abandonment certificate. *Jamestown, W. & N. W. R. Co. Abandonment*, 217 I.C.C. 739 (1937). Generally, the condition followed a finding that public convenience and necessity did not require continued operation of the line; where public need was shown for continued operation of the line, we imposed more extensive conditions. *E.g.*, see *Feather River Ry. Co. Abandonment, Acquisition*, 320 I.C.C. 417 (1964), sustained *sub nom. State of California* v. *United States*, 255 F. Supp. 475 (N.D. Cal. 1965).

Penn Central here argues in effect that we need not consider whether we can limit the right to break up the property. The bondholders as a practical matter will receive for their interest a bulk sale price from Penn Central, and the question, according to Penn Central, is merely one of fixing such a discounted price. Penn Central is correct, that as a practical matter the bondholders will receive the full economic equivalent of the liquidation value of the assets. The bulk-sale discount merely reflects a market appraisal of the risks that the estate avoids, and the bulk buyer assumes. The bondholders' position that they are entitled to a per-parcel valuation is in effect an argument that they should be free to speculate with the assets of the estate.

But Penn Central's analysis overlooks what is necessarily the bondholders' position—namely that aside from principles of equity and fairness they have a fixed right to sell off NH in parcels, so that even a bulk buyer must pay the per-parcel price. Our answer is that we may compel the bulk sale and the bulk sale discount as a condition of an abandonment certificate, and, therefore, as a reduction of the present price.

The first policy to be served in reorganization proceedings is "continued operation of the property and preservation of its unity." *First Nat. Bank* v. *Flershem*, 290 U.S. 504, 515, note 7 (1934). "In such cases, it is ordinarily necessary that the property be sold as an entirety. The unity of the systems must be preserved in both the public and the private interest." (at 526). Even if not necessary in the private interest, where there is no longer a going concern value to preserve, the public need for the rail service may require its preservation as a going concern. An appraisal of parcels does not apply "to reorganizations of railroads or corporations the continued existence of which was to the public interest." *American Brake Shoe & F. Co.* v. *Interborough R. T. Co.*, 122 F. 2d 454, 459 (2d Cir. 1941); and see *Van Schaick* v. *McCarthy*, 116 F. 2d 987, 992 (10th Cir. 1941). We, therefore, might compel NH, if it filed for abandonment, to sell in bulk and thereby make a bulk sale price appropriate. The question then becomes what is such a price.

Isolating the land receipts from the total net receipts, Penn Central presented evidence from which we can compute a minimum bulk sale discount from the fair market value of the land sold in parcels. Penn Central's testimony on this relationship involved the minimum terms that a bulk buyer must have before he can bid. Any bulk buyer would borrow at most 75 percent of

the needed capital; his best interest rate would be 9 percent; and he would finance the remaining equity at a minimum annual return of 15 percent. Each of these figures gives the benefit of the doubt to the creditors.[36]

Penn Central on brief computes a dollar discount of about $7.8 million. We approach the appropriate discount in a different way. In our view its evidence shows that the bulk sale buyer must receive a minimum return of 10.5 percent on his investment, or he will not buy. This figure derives from the data of record that 75 percent of the price must be financed at least at 9 percent, and the remaining 25 percent of the price at least at 15 percent, for a composite figure of 10.5 percent. The 10.5 percent figure means that the price must be discounted by an additional 4.5 percent over and above the 6 percent discount to present worth in order to begin to attract a bulk sale buyer. A discount of 4.5 percent on the land receipts means a discount of at least $6,695,000 computed as follows:

Year	Land receipts (1)	Land expenses[1] (2)	Net receipts (3)	Bulk sale discount Factor[2] (4)	Bulk sale discount Amount (columns 3 x 4)
	Thousands				
1	$29,099	$5,367	$23,732	.022	$522
2	38,748	5,137	33,611	.06457	2,170
3	15,909	3,253	12,656	.10529	1,333
4	10,835	1,898	8,937	.14423	1,289
5	1,823	557	1,266	.18148	230
6	7,319	2,016	5,303	.21711	1,151
Totals	103,733	18,228	85,505		6,695

[1]Excludes accrued real estate taxes, which will remain an obligation of the estate.

[2]A discount factor of 2 1/4 percent is used consistent with the assumptions of the creditors and Penn Central that cash flows accrue at mid-year. The first year's flow is assumed to occur after 6 months, and the annual rate of 4.5 percent is, therefore, a 2.25 percent semi-annual rate.

The foregoing bulk discount substantially understates what the discount would be on the open market. First, it reflects the bare

[36]The creditors argue that in the *inclusion* report we rejected a discount to present worth higher than 6 percent for the reason that the appraisals were conservative. The prior statement does not relate to the complete removal from the seller of all risk of sale in parcels which a bulk sale entails. We rejected the greater discount in the *inclusion* report only since we thought that the risk of making the parcel-by-parcel sales was adequately reflected in the appraisals and the 6 percent discount.

minimum discount of that type. We have used Penn Central's evidence of minimum financial terms, and not those terms that correspond to the risks of a 6-year liquidation of the NH. Second, Penn Central as the bulk sale buyer for continued operation experiences substantially greater risk than a buyer for a 6-year liquidation, but the discount is not increased on that account. Third, the discount is only on land although the bulk sale principle on its face would also seem to apply to the sale of the other assets in bulk rather than item by item.[37]

The limitations that lawfully may be placed on the creditors' rights to abandon and to break up the property justify reduction of at least $22,081,000 in the price.[38] This reduction is fair and equitable to the creditors. It fully recognizes, without conceding, NH's right to abandon and liquidate the estate. The net price after such reductions simply deducts from the price the equitable equivalent of the creditors' rights to less than an immediate parcel-by-parcel breakup of the railroad.

COST OF NH ASSETS TO PENN CENTRAL

We estimated the cost to Penn Central of acquiring the NH assets at $159 million in the *inclusion* report. We did not include the loss sharing or the capitalization of NH's annual losses which Penn Central would assume. Both courts have held that we erred in the computation of the cost, and our order entered today requires other changes in the computation.

The three-judge court questioned our reliance on $23 million as the cost to Penn Central of issuing bonds in that face amount, as well as our reliance on the $3.2 million representing the face amount of assumed B&P bonds (now $2.8 million). We agree that each of those amounts should reflect an appropriate discount; and we shall use $20 million as the discounted value of $23 million of bonds. Because of the revisions we are now making in several valuations, Penn Central will be required to issue $31.5 million of bonds and these will be valued at $27.4 million. The $2.8 million of B&P bonds will be discounted to $2.4 million.

The three-judge court noted that Penn Central would choose to pay the purchase price adjustments in bonds. It stated that, there-

[37] In addition, the discount should be greater, since we have employed the creditors' schedule of receipts which, as noted in footnote 34, *supra*, tends to understate the discount.

[38] Consisting of the costs of a 1-year delay of $15,386,000 and the bulk sale discount of $6,695,000.

fore, those adjustments should be discounted in computing the cost to Penn Central. We are here requiring Penn Central to offset these adjustments, including its share of the loss, against trustees' certificates in its hands. The purchase price adjustments (and loss sharing) will total $16.1 million. Since it holds $14 million of trustees' certificates, it will issue only $2.1 million of bonds for this purpose, and we shall discount that $2.1 million in computing the cost to Penn Central. To cover these bonds and the $31.5 million of bonds discussed above, we will authorize Penn Central to issue $38.6 million of bonds in lieu of the $23 million in the *inclusion* report.

The court also questioned our reliance on $22.6 of equipment obligations we thought Penn Central would assume. The court holds that Penn Central is not likely to assume $14.3 million of these obligations merely to get the continued use of the substantially lesser value of the locomotive equipment which stands as collateral for such loans. The balance of all NH equipment obligations at December 31, 1968, will be about $13.2 million. Of this amount, approximately $6.1 million, representing an excess of obligations over sale value, might be disaffirmed. Our computation of this figure is shown in appendix 2. The balance of $7.1 million represents the cost to Penn Central of assuming the obligations on that equipment which will have value exceeding the balance of the obligations against it, consistent with the ruling of the court.

We anticipated in the *inclusion* report that actual inclusion was as much as 3 years in the future, and hence provided for loans and loss sharing over a 3-year period. The three-judge court correctly states that we should have shown the burden of future annual losses of at least $8.5 million as a cost to Penn Central; but it was not an immediate cost. Discounted for the 3 years that would have elapsed under the prior findings until inclusion, the burden on Penn Central amounted to $84.1 million.[39]

Now we must increase that burden. Inclusion will now occur in less than 1 year from the date of the merger. The capitalization of future annual losses (of at least $8.5 million) discounted for only 1 year amounts to $98.1 million. The difference between the $98.1 million and the $84.1 million, or $14 million, represents the additional burden on Penn Central of early inclusion. A summary of the Penn Central's cost follows:

	Millions
Penn Central stock	$83.1
Penn Central bonds	27.4
B&P bonds	2.4

[39] $8.5 million capitalized at 8 percent and discounted by a factor of 0.7938 to reflect the fact that the burden might not arise for 3 years.

	Millions
B&P public shares	2.3
Purchase price adjustments (including loss sharing)	15.8
Cash	$8.0
Equipment obligations	7.1
Labor protection and pension costs	9.0
Harlem River Division bonds	8.9
Burden of early inclusion	14.0
Total	178.0

The foregoing computation does not include the burden of assuming NH's annual loss, which burden, consistent with the *inclusion* report, exceeds $84 million.

SUMMARY OF PRICING CONSIDERATIONS

Under the instructions of the three-judge court, we have found the liquidation value of NH is $162.7 million. We have further found that other pricing considerations require and justify a reduction of $22.1 million from the liquidation value. We find and conclude that a price that is equitable both to the estate and to Penn Central results from the $22.1 million reduction, and that NH is, therefore, entitled to consideration totalling $140.6 million (exclusive of loss sharing).

The two courts which reviewed our *inclusion* report tentatively held that the estate was entitled to liquidation value from Penn Central as a matter of constitutional law. In addition to our prior discussion, emphasizing the law and the fairness of the other pricing considerations to the creditors, a few other comments will be made regarding the lack of fairness to Penn Central of pricing NH at its immediate liquidation value on a breakup basis.

The creditors argue in these reopened proceedings that the courts have established only a floor and no ceiling on the price for the NH assets. The trustees argue that only the bondholders, and not Penn Central, have the right to contend that there should be no inclusion until price has been finally determined. They argue that as a consequence of Penn Central's acceptance of an "open-end" condition on the price for NH the price can in no event be inequitable insofar as Penn Central is concerned. The Committee makes the same argument in somewhat different terms by asserting that the Commission, the Supreme Court, and the reorganization court had an "open-end" result in mind prior to the consummation of the merger. Each of these arguments misconceives the function of the Commission in these proceedings. In valuing the estate, we cannot ignore the fairness to Penn Cen-

tral. We do not read either section 5 or section 77 to require the fairness to the estate to be determined without regard to the public interest or to the fairness to the buyer. Our prior decision was reversed on the basis of the findings and the record then before the courts. In reviewing our prior findings, the courts recognized the possible need for new evidence and precluded neither a higher nor a lower valuation than the one then before them.

The NH liquidation value is in many respects highly hypothetical insofar as Penn Central is concerned; it is a value that for the most part is unrealizable by Penn Central and frozen into the assets. Penn Central is not free to liquidate and must continue the operation of the property in the public interest. The Committee asserts that Penn Central will be able to sell the Grand Central Terminal properties. These properties now pay the heavy terminal expenses. A sale of the properties would only shift that burden onto other assets of the railroad. The capitalized excess earnings of these properties, of course, justify only a fraction of the consideration.

The creditors point to the potential savings resulting from the merger as the major justification for whatever price is fair to them or constitutionally required. This was not the intent of our decision. We did not approve the merger in order merely to satisfy the creditors of NH or even primarily to rescue NH. In Condition No. 8 we spoke of an inclusion that would be "subject to approval by the Bankruptcy Court" and would be "upon such fair and equitable terms and conditions as the Commission may impose." (327 I.C.C. at 553). We spoke, therefore, in terms of fairness to the public, and to the security-holders of both NH and Penn Central.

The primary reason for approving the merger of Penn and Central was to preserve the services of those carriers. While the provision of a home for the NH was an important consideration, particularly regarding the timing of the merger, it was not alone decisive of the merits of the merger. There were many other public interest factors supportive of the merger; and many other obligations imposed upon Penn Central as conditions to its approval. Each of these obligations is important, and together they affect a very large area of the country. A significant tapping of the annual savings to favor the NH creditors would not be in the public interest. The savings are needed to support the transportation operations of the former Penn and Central, now the country's largest transportation system.

The dollar cost to Penn Central of the inclusion will in any event greatly exceed the liquidation value of the assets. In addition to the consideration we here require Penn Central to give in exchange for the NH assets, Penn Central will assume a responsibility for annual losses which we estimated at $8.5 million in the *inclusion* report; and NH's operating deficits have now worsened.

We did not anticipate the present worsening of NH's condition in the *inclusion* report. We later show that the interim operating loss of $5.4 million that we expected Penn Central to share has now increased to $8.2 million, excluding operating expenditures in the nature of capital costs. The adjusted operating loss increased by more than 50 percent over the projected loss. The result of this trend must be that the potential burden of assuming the NH operation that we forecast in the *inclusion* report is also understated.

Part of the burden falling to Penn Central consists of its common carrier obligation to sustain essential service in the NH territory. Since we find that the operations involved are likely to be at a continuing deficit, there is a concommitant obligation on the part of State and local governments to help sustain the service. As we stated in *New York, N.H. & H. R. Co. Discontinuance of Trains*, 327 I.C.C. 151 at 222 and 223:

> In matching the *reasonable effort* of the railroads to sustain and improve essential rail passenger services, the public through its government representatives must be willing to provide a reasonable level of support for those services.
>
> * * * * * * *
>
> We believe the *reasonable level of public support* should in fact be construed as *that level of financial or other public assistance which will stimulate the carrier to initiate or, if already initiated, continue its own reasonable effort to sustain and improve essential and economically viable passenger services.*

This expectation of public support is equally applicable to NH's operations after the inclusion as before, and we have considered it as an element bearing upon the burden we here impose on Penn Central.

In the *inclusion* report, we found that the total cost to Penn Central of acquiring the assets would reach $159 million. We recognized that in addition Penn Central would be required to assume NH's loss operation in about 3 years. On the basis of the prior record, we held that it would be unfair to require Penn Central to pay a price greater than that agreed upon in the purchase agreement. Upon consideration of the supplemented record and the

rulings of the two courts which reviewed our *inclusion* decision, we increase that burden on Penn Central in the present report. We believe this increase is not undue, will not adversely affect Penn Central's ability to provide service, or impose an unreasonable burden upon its security holders.

We conclude and find that a fair and equitable, and just and reasonable, price for NH properties is $145.6 million, including a share of NH's operating losses in 1968, and we will require Penn Central to pay consideration of that amount (in the form hereinafter described) to the estate on or before January 1, 1969, the date we fix herein for inclusion of the NH.

VALUE OF THE CONSIDERATION TO NH

We approved the inclusion on the basis of Penn Central's transferring to NH several items of consideration which we valued at about $125 million. The items of consideration, and the specific values we placed on each, were the following:

	Millions
Penn Central stock (950,000 shares)	$83.1
Penn Central bonds	20.0
Cash	8.0
B&P bonds	3.0
Purchase price adjustments	9.5
Total	123.6

Our valuation has been sustained in both the three-judge court and in the reorganization court on each of these items except the last, and they require no further discussion.[40] The purchase price adjustments will be discussed briefly, before reaching the question of additional consideration.

Purchase price adjustments.—The purchase agreement provides for certain adjustments in the purchase price at closing and settlement of payment. The *inclusion* report shows that if closing had occurred on October 31, 1966, the purchase price would have been increased by $6.7 million; if the closing occurred on December 31, 1967, the NH trustees estimated that, based on an average annual adjustment favoring the NH estate since December 31, 1963, of approximately $2.3 million, the purchase price would be increased by an amount estimated to be $9.5 million.

In the present reopened proceeding the NH trustees represent the net adjustment of the purchase price as of June 30, 1968, to

[40] B&P bonds, however, should be reduced to $2.7 million (after discount) in view of recent repayments. In the reopened proceeding the creditors attacked our valuation of the stock at $87.50 per share. We note in passing that their witness was unfamiliar with Penn Central's operating and financial plans and condition; gave undue weight to extraordinary expenses of the past; and generally neglected the future prospects of the company.

be an increase of $13.4 million, including an increase of $2.3 million under section 9.2.8 of the purchase agreement for Penn Central's share of the NH adjusted net deficit (operating loss) during the period from February 1 to June 30, 1968.[41]

Assuming that closing and settlement of payment under the provisions of the purchase agreement will occur as of December 31, 1968, we estimate the purchase price adjustments pursuant to section 9 to be $16.1 million, computed as follows:

	Estimated purchase price adjustment as of December 31, 1968
	Millions
Net increase in purchase price as of June 30, 1968, exclusive of $2.3 million for adjusted net deficit from February 1 to June 30	$11.1
Estimated increase for the 11 months February 1 to December 31, 1968, for NH's share of adjusted net deficit pursuant to section 9.2.8 (11/12 of $5.5 maximum)	5.0
Total	16.1

The amount of $16.1 million purchase price adjustment includes the sales and dispositions (including retirements), and also additions and betterments, of property during the year 1964 and subsequent thereto, as well as other transactions involving property changes, under provisions of the purchase agreement. These would include changes between January 1, 1964, and December 31, 1966, the date of our valuation. The actual amount of purchase price adjustments under section 9 of the agreement will be ascertainable at closing and settlement of the purchase price. At that time such correction of the purchase price adjustments should be made as may be necessary, (1) to eliminate therefrom property sales and dispositions (including retirements) and also additions and betterments and other transactions in the years 1964 and 1965 to the extent they are already reflected in our valuation results herein; and (2) to adjust for changes in the property accounts and for other transactions which occur from June 30, 1968 to December 31, 1968. Our reservation of jurisdiction is sufficiently broad for us to permit our computing these amounts should the parties be unable to agree.

The three-judge court held that Penn Central will take "the cheaper way out," and pay the purchase price adjustments with bonds, rather than cash or stock; and that accordingly the adjust-

[41] The adjusted net deficit is computed beginning with the consummation of the Penn and Central merger effective February 1, 1968. The adjusted net deficit for the 5 months to June 30, 1968, is $3.4 million. However, section 9.2.8 fixes an annual maximum of $5.5 as Penn Central's share of the deficit. On this basis the maximum for the 5 months is $2.3 million.

ments were overstated by the amount of the discount applicable to this form of payment. Manufacturers urges that it would be incorrect to fix the amount of these adjustments at this time, and recognizes that Penn Central has the further option of paying these adjustments by canceling trustees' certificates. Since the discount was occasioned only by reason of the several options given to Penn Central to settle these adjustments, particularly the option to use bonds, we will eliminate the options and the need for most of the discount. Penn Central shall settle these adjustments under section 9 of the agreement by canceling trustees' certificates in the face amount of the adjustments before payment in bonds or other means. A discount of the purchase price adjustments will, therefore, be unnecessary and inappropriate to the extent that they are paid by cancellation of trustees' certificates.[42]

Assumption of the Harlem River Division bonds.—As a portion of the additional consideration Penn Central is to pay the estate, we shall require Penn Central to assume the Harlem River Division bonds, subject to certain conditions. In fact Penn Central and U.S. Trust are not very far apart on the conditions properly surrounding such an assumption. They now agree on the form of the mortgage and appropriate amendments to the Harlem River Indenture; our order will condition the assumption on the incorporation of those amendments into the indenture. U.S. Trust urges the adoption of the suggestions of the reorganization court that sinking fund payments and interest thereon and on overdue interest be eliminated, and accrued interest be paid in four installments.

The principal and accrued interest of these bonds amounts to about $8.9 million; the principal of $6.6 million matures in 1973. Penn Central offers to carve out a separate issue of bonds from the purchase agreement with a first lien on the Harlem River Division in the aggregate principal amount of $9.65 million. We believe the divisional first mortgage for the 5 percent 25-year bonds, which Penn Central will issue, subject to the minor modifications suggested in the brief of U.S. Trust, should serve as a supplemental indenture for the Harlem River bonds; and that Penn Central should assume the Harlem River bonds subject to the following additional terms: (1) payment of 20 percent of the accrued interest upon assumption and 20 percent in each of the next 4 years; (2) elimination of sinking fund; (3) no acceleration

[42]Since Penn Central holds $14 million of trustees' certificates, the purchase price adjustments of $16.1 million will be paid by cancellation of these certificates and $2.1 million of bonds. The discounted value of the bonds is $1.8 million.

of maturity because of past defaults; (4) no interest on overdue sinking fund payments or, for the period prior to assumption, on overdue interest; and (5) an option to refinance the principal amount at maturity with the issuance of 5 percent 25-year bonds in the face amount of $7.6 million. The present interest rate on this issue of bonds is low, and with the sinking fund requirements eliminated, no undue burden would fall on Penn Central.

Summary.– Penn Central urges that any further consideration paid by it to the estate should be in the form of bonds, rather than stock or cash. We agree. We have found an adjusted valuation for which the estate is entitled to be paid that totals $140.6 million. In addition we have imposed on Penn Central the requirement that it pay $5 million of the NH's 1968 operating losses. Accordingly the consideration to be received by the NH estate from Penn Central should be valued as follows:

	Millions
Penn Central stock (958,000 shares)	$83.1
Penn Central bonds	27.4
Cash	8.0
Assumption of Harlem River Division bonds	8.9
B&P bonds	2.4
Purchase price adjustments, discounted (including loss sharing)	15.8
Total	145.6

The foregoing computation will require the transfer of $31.5 million in bonds to the estate, rather than $23 million referred to in the *inclusion* report.[43]

INTERIM SUPPORT

The *inclusion* report provided for a $25 million loan from Penn Central to NH over a period of 3 years. The loan would be taken down with the approval of the reorganization court whenever NH's cash balance fell below $5 million. The report also provided for loss-sharing by Penn Central under which it would bear 100 percent of an adjusted operating deficit in the first year, 50 percent in the second, and 25 percent in the third, up to a maximum of $5.5 million in any year. The three-judge court held that we were not bound to require Penn Central to absorb all NH's operating losses subsequent to the merger, that we were justified in setting a ceiling on Penn Central's participation in losses and in providing that it bear only a fractional share. The court sustained the loan arrangement, and set aside the formula solely on the grounds that

[43] In addition, Penn Central will issue $2.1 million of bonds as part payment of the purchase price adjustments.

the desire to curtail litigation was an insufficient reason for the downward progression in Penn Central's share of the losses.

Our order today requires inclusion by the end of this year. Penn Central will absorb the entire loss thereafter, and upon inclusion the loan provisions will become inoperative. The interim support which remains for consideration is for the 11-month period since the consummation of the merger on February 1, 1968, until December 31, 1968.

The three-judge court has correctly stated that we predicated the loss sharing formula of the *inclusion* report upon the view that NH's fortunes had reached their nadir in 1967, and that the outlook for 1968 and beyond was somewhat less dismal. NH's third quarterly report filed with the Commission on October 28, 1968, while indeed dismal is not radically more dismal than the figures for 1967. In 1968, operating revenues in fact increased over 1967; operating expenses also increased so that net railway operating income for the first three quarters was a deficit of $18.76 million, or $1.5 million more in the red than for the same period in 1967.

The more startling aspect of the NH operation for 1968, actual and projected, has been its requirement for large takedowns of the Penn Central loan. The takedowns total $14 million for the year of the total available amount of $25 million. The total, which was expected to last for 3 years, would at the present rate of takedown be entirely drawn down by June of 1969, or 1 1/2 years from the consummation of the merger. The decline in NH's cash position is starkly shown in the following table:

NH CASH FLOW ANALYSIS[44]

	1967	1968
	Thousands	
Total receipts	$201,721	$195,839
Total disbursements	208,381	211,511
Net	(6,660)	(15,672)

The 1967 receipts were augmented by several nonoperating income items, such as $500,000 in interest payments from Providence

[44]Reported 1967 figures; reported January-August 1968 figures; and NH's estimated figures for September-December 1968. All receipts figures exclude trustees' certificates and takedowns from the court registry.

Produce Warehouse, a wholly owned subsidiary; and $1,008,425 from Boston Terminal Corporation in repayment of past advances. The estate also received over $500,000 from the United States Department of Transportation to reimburse it for maintenance-of-way expenditures incurred in connection with a proposed high-speed rail demonstration on NH's lines. These items were not available in 1968. In addition, the operating loss estimated for 1968 is higher than in 1967 as wages and related expenses advanced.

The creditors ask that we require Penn Central to absorb the entire cash deficit for 1968—or from February 1, 1968, when the merger was consummated, to the end of the year. We believe this would be inequitable to Penn Central for several reasons. First, the cash loss is occasioned by other capital charges that we held in the *inclusion* report Penn Central should not be required to pay; the present request of the bondholders in part merely seeks to reopen that question.

Second, as the operating losses increase, Penn Central's share of the losses also increase under the formula up to a maximum of $5.5 million in any 1 year. The maximum is not an effective limitation on Penn Central's 1968 share; for, if we were to accept the suggestion of the three-judge court and require a 50–50 split of the 1968 loss, Penn Central would pay less than the maximum it must now pay under the formula. Of the $15.7 million cash deficit for 1968, the operating loss amounted to $8.2 million, estimated as follows:

ESTIMATED NH OPERATING DEFICIT—1968

		Reported 5 months 1968	Estimated 12 months 1968
		Millions	
Net railway operating deficit		$9.4	
Less: Depreciation	$3.3		
Retirements	0.2	3.5	
		5.9	
Less: nonoperating income (after taxes)		2.5	
Adjusted net deficit		3.4	
Projected net deficit (as adjusted) (12/5 x $3.4)			$8.2

In the *inclusion* report we explained that the burdens of the interim period prior to inclusion should in fairness be borne in part by the States, in part by Penn Central, and in part by the estate. The events of the intervening months do not convince us that we should impose NH's entire operating loss for 1968 on Penn Central, nor have the courts required that result. We adhere to requiring Penn Central to absorb all of the 1968 operating loss up to a maximum of $5.5 million per year. The sum of $5 million (for 11 months) has been included in the purchase price adjustments discussed earlier as an increase in the purchase price pursuant to the *inclusion* report and the purchase agreement.

INCLUSION OF NH ON JANUARY 1, 1969

Time is fast running out for NH. This rail complex, whose passenger service we have found to be an essential component of the commerce of New England, and whose freight operations we regard as vital to that area's economy,[45] now subsists with a cash balance less than adequate to meet one average week's disbursements. Projections based on existing traffic revenues indicate that notwithstanding the $4 million loan takedown approved in October 1968, NH's cash balance in January 1969 will be about $1.4 million, less than a third of its November balance. But for the Penn Central loan arrangement NH would long since have gone under, and without another takedown early in 1969 it cannot continue to operate. The reorganization court, in unmistakable terms, has made it clear that absent an inclusion order by this Commission no such further borrowing by NH will be permitted.

Penn Central asked in its opening brief whether the creditors retained a right of "reversion" if it should eventually be found by the Commission and the courts that the price was too high for Penn Central to pay. Certain creditors have responded that there is no possibility of reversion "if, but only if" the Commission adopts liquidation value as its standard. If we do not adopt liquidation value as our standard, presumably the creditors threaten to block inclusion.

We disagree with the position of those creditor interests which argue that the reorganization court cannot require the creditors to surrender their liens unless they are assured of receiving

[45] See *New York, N. H. & H. R. Co., Discontinuance of Trains*, 327 I.C.C. 151, and see our *reconsideration* report herein.

liquidation value (with piecemeal sales beginning immediately) of the NH assets. Section 77 calls for a fair and equitable price; it does not prescribe liquidation value. The valuation standards of the Interstate Commerce Act do not refer to liquidation value; and section 5 refers only to just and reasonable or equitable terms. The Constitution, as we have discussed earlier, does not prescribe liquidation value as an irreducible minimum.

The NH creditors are guaranteed just and reasonable compensation and other terms for their interests in the NH, whenever distribution of the compensation shall occur, whether at the time of or after the properties pass to Penn Central. Since Penn Central must include the NH and must pay a price just and reasonable to all concerned, the creditors lose nothing, vis-a-vis Penn Central, by having their liens transferred from the NH properties to the consideration which Penn Central will eventually have to pay.

A total abandonment of the NH would be inconsistent with the public interest. Consequently, a liquidation in fact is not an option open to us. But continued operation of the NH under the *status quo* would likewise be intolerable, as the reorganization court has held. Operation by Penn Central, on the other hand, provides a feasible and achievable alternative. Yet, in order for Penn Central to effectively rescue the NH operations, it must be free to conduct them according to the dictates of good and efficient management as an integrated part of its own system. This it cannot do if it must take the NH properties without the power of disposition over them and subject to the creditors' liens.

It is clear that liquidation values of the magnitude sought by the creditors are unfair to Penn Central, and would render inclusion unfeasible. Such values would provide unfair and inequitable terms and would not fall within the scope of Condition No. 8 of appendix A of the *merger* report. But just as the briefs of the creditors are replete with exaggerated claims, the Penn Central briefs contain exaggerated fears.

We do not reach many of the questions on early inclusion that Penn Central raises primarily because we disagree with one of its basic premises—the premise that the courts may reach a price as a matter of law that will be unfair to Penn Central. The NH estate has no such right. To ignore Penn Central's interest under the statutes or the Constitution would be to ignore the public interest in preserving NH service; if the price required in law for NH is so high that we would be compelled to hold it unfair to

Penn Central the result would be to deny the public need for the service. Whether we view the interests of the estate or the rights of the creditors, we are of the view that the Constitution requires but a fair price, and that such a price cannot in logic or law be divorced from what is fair to Penn Central.

Penn Central in effect asks us to stay inclusion until the price has been judicially reviewed. We deny the request, based on our view of the law governing price and the NH's deteriorating cash position. In our view the inclusion should not be delayed pending judicial review of either price or the reorganization plan. The primary consideration is the public interest, and in the present context, the continuance of NH service without interruption is a public interest matter of paramount importance. A takeover should occur on January 1, 1969, even in view of the high probability that litigation will continue beyond that date over the price and other terms of the inclusion. Such a takeover is fully within Penn Central's capacity and competence, notwithstanding the burdens of an assumption of operating losses and a payment of consideration in the interim. Our order hereinafter provides for the inclusion of NH and its affiliates and subsidiaries in Penn Central effective January 1, 1969, under terms and conditions which we believe reflect the equities of the parties, and adequately preserve their rights pending final adjudication of appeals taken or to be taken from our order under section 5, and our approval of a plan of reorganization for the NH.

It must be emphasized that by inclusion we contemplate nothing less than a binding transfer to Penn Central, free and clear of all liens and encumbrances, of all the assets of NH proposed to be transferred under the agreement between Penn Central and NH, as amended, and the concurrent payment to the NH trustees of the consideration which we have here found to be fair and equitable. In the *inclusion* report we stated our reasons for rejection of the then-considered lease arrangement as patently unfair. At the present stage of these proceedings even less justification exists for any concept of an interim inclusion, whatever the means employed.

Our order in the *inclusion* report approved the basic steps for accomplishing physical inclusion of NH as outlined in the first step of the reorganization plan. Few changes are needed to update the mechanics of closing. As requested by the trustees, December 31, 1968, will be designated the closing date, in lieu of the last business day of the calendar month following the month

in which the regulatory and judicial orders approving the transactions become final. On January 1, 1969, subject to the approval of the reorganization court, the NH properties enumerated in paragraph 3 of the Penn Central-New Haven agreement will be transferred to Penn Central, and the trustees will receive the entire consideration specified in paragraph 6, as herein adjusted. This would accord with the sense of our decision herein, that consummation of the section 5 transaction be so effected as to permit operation of NH, effective January 1, 1969, as an integral part of the Penn Central system.

Penn Central insists, however, that if the B&P reorganization has not been consummated by that date, inclusion should be conditioned upon the valid and irrevocable transfer to Penn Central of NH's rights over the B&P line. It is sufficient for the purposes of this transaction that Penn Central succeed to NH's rights in the B&P reorganization and, subject to the approval of the reorganization court, be required to operate in lieu of NH over the B&P line. Our reservation of jurisdiction herein will insure that Penn Central will succeed as well to New Haven's B&P property rights when the B&P plan is in fact consummated, or enable us to make appropriate adjustments with respect thereto if necessary.

The trustees request, also, that the post-closing date, under the plan the last business day of the fifth calendar month subsequent to the month in which the closing takes place, be postponed indefinitely to a date to be thereafter fixed by the Commission, so as to permit a single post-closing adjustment of all accounts after final court review. Evidence of record indicates, as stated, that the purchase price adjustments under the purchase agreement will result in a favorable balance to NH, but that post-closing adjustments, under which Penn Central assumes NH's current liabilities, will reflect a substantial balance in favor of Penn Central.[46] A requirement that Penn Central assume indefinitely this negative balance is not warranted, and we hereby require post-closing adjustment as provided in the agreement. Sections 11, 12, and 13 of the purchase agreement and the modifications thereof recommended by the trustees are not necessary to this transaction and should not be adhered to by the parties. As requested by the trustees, interest on the

[46] The trustees estimate that as of June 30, 1968, the post-closing adjustments under section 7 of the purchase agreement will total $8.2 million. See appendix 7.

trustees' certificates held by Penn Central will cease to accrue after December 31, 1968, since the principal amount represented thereby will have been reflected as an offset to the purchase price adjustments.

PROTECTION OF EL TRAFFIC AT MAYBROOK

In the *inclusion* report we denied EL's request for special conditions to protect the interchange of traffic it has developed with the NH at Maybrook, N. Y. The three-judge court did not sustain us, pointing out weaknesses in our reasons and concluding that our report offered "neither an analysis of the anti-competitive effect of inclusion without protective conditions nor convincing evidence that the pre-existing coordination with EL will be maintained." It noted that the policies of the antitrust laws should be conscientiously applied, and included in its remand the admonition that EL's request be reconsidered.

On reconsideration and on the basis of the record supplemented by evidence on further hearing, we have concluded that El should be accorded protection substantially like that provided for CNJ, Reading and WM in revised appendix I of the *inclusion* report. Because of changes in terminology, tailoring the conditions to fit EL's situation, and other modifications—discussed below—we have separately set forth in appendix 3 hereto the terms for EL's protection.

EL is itself a large trunkline carrier with more than 3,000 miles of road extending between Chicago and the eastern seaboard. Effective April 1, 1968, it was integrated, as a wholly owned subsidiary, into the N&W system which ranges for more than 11,300 miles across the territory extending from the eastern seaboard as far west as Omaha, Nebr. The N&W system and Penn Central are the two largest rail systems in the eastern part of the country, and they are major competitors throughout the greater part of their territories. Moreover, they vie with each other, and the CNJ-C&O-B&O lines, for traffic which EL and NH have been interchanging at Maybrook.

Though a part of the N&W system, EL remains a separate corporation responsible for servicing its very considerable debt. To some extent it competes against other lines of the N&W system.

At the hearing on remand EL showed that, during the first 6 months of 1968, it interlined with NH about 53,000 cars originating or terminating at NH points, producing about $11.9 million

of EL revenue. This constitutes some 10 percent of EL's total railway operating revenues—which amounted to $119.5 million for the first half of 1968, and $223.8 million for the whole of 1967. About 99 percent of the study traffic was interlined at Maybrook. The volume and revenue figures understate the total interline because the study on which they are based does not include traffic overhead to NH and because the volume of this interline traffic is usually less in the first half-year than the second half-year. In 1966, NH interlined 124,435 cars with EL at Maybrook, as compared to 102,980 interlined with Penn at New York Harbor and 97,391 with CNJ at Maybrook.

Twenty-three percent of the EL-NH interline traffic in the 1968 study was to or from points in southern New England (Massachusetts, Connecticut, and Rhode Island) common with the B&M, namely, Boston, Lowell, West Concord, Fitchburg, Clinton, Worcester, Springfield, Holyoke, and East Hampton. About 75 percent was overhead to EL and about 65 percent to or from western and southwestern carriers. Almost 55 percent of this traffic was interlined by EL at Chicago, and 27 percent at Buffalo. While EL disavows that its evidence on this traffic is an attempt to show susceptibility to diversion, it does point out that overhead traffic, as we acknowledged in the *inclusion* report, is in general more vulnerable to diversion than origin and destination traffic.

The EL study shows that 9 percent of the traffic originates or terminates on the lines of its affiliates, but it does not show what portion is overhead to the affiliates. It is reasonable to conclude, however, that a substantial part of the 27 percent interchanged at Buffalo is received from N&W (since that point is N&W's northeastern terminus), and that much of the 55 percent interlined at Chicago is to and from N&W and its western connections. EL has expedited access to western territory via N&W through special arrangements with the Union Pacific under which traffic can be routed via Decatur, Ill., on through trains to and from North Platte, Nebr., 733 miles, bypassing St. Louis, with crew change at Kansas City but with through motive power. At North Platte connection is available for Cheyenne, Wyo., Ogden, and Salt Lake City, Utah, and points in California and the northwest.

Both N&W and EL maintain solicitation forces beyond their lines at many major traffic generating points in the west and southwest. These off-line solicitors and other factors favorable

to EL and N&W heavily influence the quantity of interline traffic at Maybrook; three-fourths of that traffic is eastbound from EL to NH.

Less than 1 percent of the revenues ($67,000 of $11.9 million) in the EL study was derived from interline at Binghamton, N. Y., presumably from the N&W, EL, D&H, and B&M through route to and from Boston. That amount undoubtedly falls short of the Binghamton interchange's total yield to EL, however, since, as to that route, the traffic study was restricted to traffic to and from NH points common with B&M, and did not include traffic to and from points beyond the NH, which would be NH overhead traffic.

It was brought out on the record that EL has recently joined in the establishment of two expedited east-west through routes which should improve EL's Binghamton interchange and enhance EL's competitive status. One is between Chicago and Boston via EL-Binghamton—D&H-Mechanicville—B&M, offering second-morning delivery in Boston with through motive power and an elapsed time of either 30 hours and 45 minutes or 34 1/2 hours (the record is not clear on the time). The other is an N&W system route providing 49-hour service from Kansas City, Mo., to Jersey City, N.J., without change of locomotive, which sets off cars at Binghamton for pick-up by EL's Chicago to Boston train. In addition, effective August 23, 1968, EL succeeded in reducing the number of crew-change points from nine to six on its trains between Chicago and Jersey City.

EL provided a comparison of service routes between Chicago and several eastern points as an indication of its and CNJ's ability to compete with Penn Central service. In most instances Penn Central's single-line service offered the shortest scheduled time, but in other instances the times via EL's routes or CNJ's routes were the shortest. For example, on TOFC service from Chicago to Boston, the time via Penn Central is about 28 hours compared with 42 hours and 15 minutes via EL and NH through Maybrook, and 30 3/4 to 34 1/2 hours via EL, D&H, and B&M through Mechanicville. From Chicago to Providence, however, the time for Penn Central's general merchandise train is 48 hours, only 15 minutes less than the scheduled time over the route of the CNJ; from Chicago to New Haven, Penn Central's general merchandise train takes 55 1/2 hours, compared to 34 1/2 hours via EL's route and 42 hours via CNJ's.

Besides showing that Penn Central has the fastest service over most of the routes shown, the comparison shows several other things, among them that (1) Penn Central does not offer the fastest service to or from all points in southern New England but rather that, between certain points, the other carriers are equally fast or faster; (2) there is room for improvement in the service of each route; and (3) the existence, side-by-side, of routes having such widely disparate elapsed times indicates that, as to some traffic, speed is not determinative of routing, and that factors other than speed influence the selection of routing. EL's expert witness agreed that there are many other factors which influence routing, and that speed, while very important, is not necessarily controlling. Among the other governing factors given were: train schedules, service dependability and frequency, equipment availability, carrier solicitation, shipper allocation, transit privileges, rates and shipper plant location in relation to originating or terminating railroad. An example of a routing factor affecting the flow of traffic at Maybrook is the low clearance on part of the NH which precludes the movement of trilevel automobile rack cars and large trailers in TOFC service.

The approval given the Penn Central merger and the N&W merger and inclusions rested in part upon the potential in those transactions for bringing about better, faster, more economical service and improved equipment availability. Penn Central, besides inaugurating faster schedules in single-line service to and from southern New England, has recently begun operations at a large electronic yard at Selkirk near Albany, N. Y., where it plans to make up through trains for expedited movement between major cities in its territory and to break up eastbound trains for distribution of cars to northeastern points, including points in southern New England served by NH. It has already implemented some of its plans for this territory when it recently called upon NH to switch the eastern interchange point on traffic to and from points west of Pittsburgh, Pa., from Greenville Pier in New York Harbor to points common to NH and Penn Central on the line between Boston and Albany (the B&A line), for example, Boston, Framingham, Worcester, and Springfield.

EL looks upon this recent step as a sure sign that Penn Central plans to upgrade the NH lines between points on the B&A line and NH points in southern New England not served by Penn Central and make it more difficult for EL to compete via Maybrook

routing. Such upgrading could have a deleterious effect on the Maybrook interchange by drawing traffic to the B&A line on the strength of better service. In some respects, however, that would work to the advantage of the N&W system, especially if B&M is included therein, for the N&W would have both its long haul and the benefits of Penn Central's upgraded facilities. In view of N&W's special interline arrangement with B&M, this advantage would still accrue to N&W without B&M inclusion, but perhaps to a lesser degree, depending on B&M's willingness to remain cooperative in the N&W arrangement, and on its capacity to maintain the needed quality of service.

The major alternate routings, on the east-west traffic of southern New England are (1) NH, EL, (2) NH, Penn Central, (3) NH, CNJ and connections, (4) as to the substantial traffic of Boston and the several commercial and industrial centers along the B&A line, B&M, N&W system, and (5) the potential route to and from NH territory via NH, B&M, N&W system. It is apparent that to the extent Penn Central might promote (1), it detracts from all the others including its own long haul on (2). To the extent it promotes (2) by upgrading NH facilities, it would benefit its major competitor on (5). It is also apparent that N&W has significant influence over (1), (4), and (5), all in competition or potential competition with each other; and is in a position to take countermeasures against Penn Central efforts to promote (1).

EL is requesting protection and active promotion of (1) which maximizes its length of haul and revenues. Specifically, EL is asking for conditions which provide that whenever Penn Central upgrades any of its system routes competitive with (1) (the EL-NH Maybrook route), or takes other action to promote those routes, it must take commensurate action as to route (1). Such conditions could obligate Penn Central, in the event it wanted to upgrade other routes, to make capital expenditures on route (1) with no contribution from EL, and no assurance from N&W that the route west of Maybrook would be comparably upgraded or maintained or even that the N&W system would permit continued cooperation in maintaining the quality of service on its segment of the route. Such conditions could also obligate Penn Central, in the process of the upgrading, to eliminate the low clearance handicaps now present on the Maybrook route.

EL's requested upgrading condition exceeds the protection granted CNJ, Reading and WM in appendix I. Those conditions

merely require Penn Central and the three smaller lines to "maintain and keep open *** fast competitive service routes via existing or comparable junctions or gateways," such as Maybrook. There is no requirement for continuous improvement of the service beyond the level of the service at the time of NH's inclusion.

Both the Penn Central merger and the N&W merger and inclusions were found consistent with the public interest because, at least in part, they provide the means by which transportation economies can be effected and improvements can be gained in transportation service. Increasing Penn Central's already great obligations by the additional upgrading requirements sought by EL would tend to discourage Penn Central from upgrading its own services or any part of the NH plant and services; and that would be contrary to our objective in the Penn Central merger and the NH inclusion.

By the same token, a breakdown of EL's Maybrook route would be contrary to our purpose in EL's inclusion in N&W. The viability of EL and the preservation of its service throughout its territory are matters of public interest and their frustration would be inconsistent with the public interest. We are convinced that by virtue of the substantial yield of the Maybrook route to EL, the atrophy of that route would be a serious blow to EL and the national transportation system.

We conclude that the solution to the problem lies in conditions which would preserve the present quality of Maybrook route service and at the same time leave the way open for Penn Central to maximize the efficiency of its own routes via NH. The NH's inclusion is the first step in that direction. Additional steps would be conditions to preclude Penn Central from downgrading the interline service with EL at Maybrook. This, we believe, will create a climate of intramodal competition for New England traffic which should generate improved transportation service on the part of N&W, EL, Penn Central and the other carriers which vie for that traffic.

Under the doctrine of *McLean Trucking Co.* v. *United States*, 321 U.S. 67, 87, we are required, in our determination, to give consideration to the effect of the NH inclusion on competitors and on the general competitive situation in the railroad industry in the light of the objectives of the national transportation policy. In this case, we have carefully estimated the scope and evaluated the effects of the curtailment of competition that

may result from the inclusion of NH in the Penn Central system. While the NH inclusion will undoubtedly assist in effectuating the overall transportation policy, adjustments in the form of protective conditions for competing railroads become necessary in order that we may properly accommodate the provisions of section 5(2) and the federal antitrust legislation. *Minneapolis & St. Louis R. Co. v. United States*, 361 U.S. 173.

In the absence of additional protective conditions, not only southern New England but also points west thereof would, to some extent, experience a lessening of competitive rail transportation. On the other hand, the imposition of conditions to maintain insofar as possible the status quo of Maybrook, will preserve EL's opportunity to compete for traffic to and from southern New England and areas west thereof as it existed prior to the NH inclusion. But the conditions should not be so onerous as to discourage Penn Central from improving generally the rail service of NH territory.

Penn Central, though opposed to increasing EL's protection, has indicated in the alternative a willingness to accept the revised appendix I conditions with modifications. Both carriers are willing to accept certain changes, reflected in appendix 3, such as naming EL as the protected carrier, making the conditions effective as of the date of the NH inclusion, eliminating Penn Central's obligation under section 8 to preferentially solicit for the Maybrook route, and making the appeal remedy of section 12 available to Penn Central as well as EL. All the agreed changes are clearly appropriate and are made in the conditions here being imposed.

Important modifications are contested, however. Penn Central wants the protection to be terminated upon the merger of EL into a major system or upon the merger of N&W with C&O. EL, pointing to the view expressed by the three-judge court, proposes that the protection be made subject to reconsideration upon the happening of those contingencies. As we view our obligations and powers under the act, we must maintain a constant surveillance of the transportation system and govern our decisions in accordance with its changing needs. We cannot, from our present vantage point, adequately see how an EL merger or an N&W-C&O merger at some indeterminate future time will affect the EL system, and, therefore, we are hardly in a position to find that either event will automatically end EL's need for this protection. Moreover, leaving the matter generally open for

reconsideration will permit us to re-examine the need for the protection.

As to the upgrading requirement sought by EL, we have already indicated how it would tend to defeat the purpose of the NH inclusion. As much as the public interest requires the protection of EL's Maybrook route, it also requires an improved NH, and we are therefore not inclined to impose a burden which would promote the former to the neglect of the latter. Furthermore, retaining jurisdiction to reconsider the protective conditions will stand as a deterrent against Penn Central's taking steps toward rendering the EL Maybrook route noncompetitive. In this regard, it should be noted that Penn Central moved to upgrade the Maybrook route by seeking trackage rights to Maybrook over the Lehigh and Hudson River Railway, but was unsuccessful when the directors of the latter failed by a three to three vote to approve the arrangement. The representative of EL, one of the owners, voted in the negative.

The conditions in the *inclusion* report require Penn Central to concur in competitive rates on traffic handled jointly by NH and the protected carriers. Penn Central would have us limit this requirement as to EL to rates "to and from points presently local to the New Haven." This limitation would free Penn Central to refuse concurrence in joint rates on NH overhead traffic. The reason given is that, with its expedited service via B&M, the N&W system does not need protection as to these rates. This limitation would also permit Penn Central to bypass NH routes altogether on traffic to and from points north and east of the B&A line. We do not believe the limitation should be included, because it would leave some of EL's Maybrook traffic unprotected, and, in any event, Penn Central would still benefit to the extent the traffic moves across NH territory.

EL asks for removal of the words "insofar as such matters are within its control" from sections 2, 3, 4, 6, and 7 of revised appendix I. It views these words as applying only to *force majeure* situations. EL's view is too limited and its request is therefore denied. It must be recognized that the success of through routes and joint rates depends upon cooperative effort by all participating carriers.

Section 3 requires that present "traffic" and operating relationships shall be continued; and section 6 requires that each carrier participating in a through route shall cooperate with the other participants and "shall use its best efforts with its

connections to obtain similar cooperation" in order to continue the route as a competitive route. Penn Central seeks to have the quoted words deleted, contending they impose an obligation tantamount to soliciting. These words do not impose any obligation relating to the solicitation of traffic. They refer wholly to operations and operating practices. Our traffic conditions would serve little purpose if, while the Penn Central system and EL exerted adequate effort toward success, other connecting carriers lagged in their effort. Penn Central should seek cooperation from those connections to the extent necessary to maintain the present level and quality of service on the protected routes.

In consideration of what has been heretofore explained, we find it just and reasonable that EL's routing via Maybrook and NH shall be protected in accordance with the terms set forth in appendix 3.

PROTECTION OF CNJ

CNJ, on brief, brings into this phase of the proceeding for the first time a request for conditions requiring Penn Central to pay it revenue indemnities as an allegedly essential supplement to the traffic conditions prescribed in the *inclusion* report. In support, it has offered neither evidence nor argument not already considered by us in arriving at the prescribed conditions. It did state in a letter to the Commission (of April 24, 1968) accepting the prescribed protective conditions that it was negotiating with Penn Central for revenue indemnification and that if negotiations were to fail, it was "prepared to challenge" our prior reports.

On the question of CNJ protection, the record now before us is not materially different from that on which the *inclusion* report was predicated. The protective conditions of that report provide a means by which modification may be obtained where necessary. Therefore, in view of the record, the conditions already imposed to maintain the flow of traffic via existing gateways, the limited scope of the remand and our present conviction that inclusion of NH in Penn Central will not adversely affect CNJ to a significant degree, if at all, we deny CNJ's request for conditions prescribing revenue indemnification.

INCLUSION OF LEASED LINES OF NH

Inclusion of Providence and Worcester Railroad Company.—In the *inclusion* report, we deferred passing on the Providence and

Worcester Railroad Company's (P&W) request for inclusion in Penn Central. P&W is 50.16 miles long with 113.53 miles of track. Its main line extends 43 miles from Providence, R. I., to Worcester, Mass., and it also has a branch line from Valley Falls to East Providence, R. I. Pursuant to a 99-year lease effective July 1, 1892, P&W demised all its properties, rights, franchises, and privileges to NH. The latter pays annual rental of $426,868, comprised of $2.50 per share dividend on P&W's capital stock, interest on P&W's bonded indebtedness, and all taxes imposed on P&W.

There are 24 stations on the lines of the P&W, 11 in Massachusetts and 13 in Rhode Island. The population of the area served approximates 656,000 persons. Situated in cities and towns served by the P&W lines are 10,000 construction and manufacturing firms employing 140,000 persons. At this time a freight only service is operated, consisting of one round trip, through service, 5 days a week, one local freight train, and switching service at Woonsocket, R. I., and at each terminus.

By amendment to their plan of reorganization the trustees reject the lease with P&W.[47] P&W claims that the lease is beneficial to the NH, and accordingly, cannot be rejected. Among other things, P&W. points out that in pleadings filed with the reorganization court, dated December 4, 1963, and June 29, 1964, the trustees stated that it is in the best interest of the estate that the lease be affirmed.

The plan of reorganization for NH contemplates that it will cease to operate as a railroad. Therefore, the reorganized company would have no use for the P&W facilities or the lease authorizing the use of those facilities. And Penn Central, as purchaser of the NH assets, does not wish to be an assignee of the lease. Obviously for the trustee to affirm the lease in these circumstances would be an improvident and burdensome undertaking, and its rejection is proper. The fact that the trustees have rejected the lease at Penn Central's request does not derogate from the right to take such action.

We turn now to P&W's petition, filed May 3, 1967, for inclusion in Penn Central as a leased line under the terms and conditions of P&W's existing lease with NH. P&W contends that it is an integral part of the NH system and would be an even more vital

[47] Under section 77(b)(5) of the Bankruptcy Act, "A plan of reorganization * * * may reject contracts of the debtor which are executory in whole or in part, including unexpired leases * * *."

link in Penn Central. Furthermore, P&W claims that unless it is included in Penn Central, it will be vulnerable to diversion of traffic with the result that its service may be destroyed.

Penn Central concedes that when we found in our report and order of April 6, 1966, "that inclusion of New Haven's freight and passenger operations in this transaction will be consistent with the public interest, and our approval of the /Penn Central/ merger is conditioned upon such inclusion," (327 I.C.C. at 526-527), the P&W lines were embraced in the operations to be included. However, Penn Central maintains that when NH becomes part of its system, operation over P&W will be unnecessary, uneconomical, and a burden to it, and that it intends to file an application to abandon operation over the line of P&W. It asserts that if we find abandonment is not warranted, we have the power to fix reasonable terms and conditions for the continued operation.

P&W contends that it is worth at least $6.4 million in annual system income to Penn Central if the latter should acquire P&W on the same terms as are contained in the P&W-NH lease. P&W further contends that if is not included in Penn Central, P&W will suffer annual diversion of $426,110, which would constitute a substantial percentage of revenues applicable to traffic over its line. Penn Central has not attempted to rebut the contentions of P&W. Rather it avers that evidence submitted by P&W has no probative value.

On this record there is the probability of substantial diversion of traffic from P&W. We find that the continuance of P&W's service is in the public interest, and that failure to include P&W in the Penn Central system would have a serious, adverse effect on P&W and on the shipping public dependent upon its service.

Penn Central asks that we provide that P&W be operated by Penn Central without a lease and for the account of P&W until we determine whether or not P&W may be abandoned. Penn Central contends that if P&W is included under the terms it seeks, Penn Central would be assuming all present claims of P&W against NH arising under its lease as well as all claims arising under the termination provision of the lease. It argues that these claims presently exist and are substantial in amount. It also argues that if the lease is terminated prior to its 1991 expiration date without P&W approval, Penn Central may be liable to P&W for damages, that the lease terms are onerous and, in view of the disputes between P&W and NH, uncertain.

Penn Central also contends that it would be required to assume the Providence Terminal Agreement of 1935 relating to the use of certain railroad operating property in the Providence-Pawtucket area. It argues that this agreement has never received Commission approval and is so drafted that it cannot be determined what its terms are and whether they would be fair and reasonable to Penn Central.

Penn Central also objects to the provision in the P&W charter to the effect that no stockholder may vote more than one-fourth of the outstanding stock of the corporation. Therefore, Penn Central, after acquiring NH's shares of P&W would not be able to include P&W in its consolidated tax return unless it could eventually acquire 100 percent of P&W's stock. It asserts also that it would be very difficult to simplify the Penn Central corporate structure by acquiring P&W by merger or purchase since a relatively few holders of P&W stock would be able to veto the terms of any such transaction and hold out for better terms. It contends that if the P&W property is to be leased by Penn Central, P&W should, in connection with submission of the lease to its stockholders, also submit to them a proposal to amend its certificate of incorporation to eliminate the stock voting provision about which Penn Central complains.

Penn Central's arguments against leasing P&W are not altogether material. In agreeing to include all of NH, Penn Central did not exclude the various disputes in which NH is involved with P&W or the claims of P&W arising therefrom. Such disputes and claims will become the responsibility of Penn Central whether or not it becomes the lessee of P&W. The same thing applies to the voting rights to P&W stock. They will be held by Penn Central after NH's inclusion and Penn Central will be under the same disability with regard to its rights to vote P&W whether P&W is operated as Penn Central proposes or whether it is operated under the lease as it proposes.

In requesting that we provide for Penn Central operation without a lease of P&W until we determine whether or not the latter company may be abandoned, Penn Central is in effect asking us to defer action on P&W's inclusion until Penn Central can file an application for its abandonment. The P&W petition was timely filed and has been supported by probative evidence. The treatment requested by Penn Central is not justified. Penn Central's request is denied.

We find inclusion of P&W in Penn Central consistent with the public interest. Inclusion will benefit Penn Central and assure

adequate transportation service to the shipping public. Failure to include P&W in Penn Central would jeopardize the service available to the public in the areas served by P&W.

As regards the terms of such inclusion, the provisions of the lease from P&W to NH constitute equitable terms except to the extent they prescribe that the lease shall remain effective through June 30, 1991. We do not find it fair to bind Penn Central to a lease of such duration. If at some time before the lease would expire by its terms, Penn Central believes that the public convenience and necessity no longer require operation of P&W, Penn Central may file an appropriate application for abandonment authority. We express no opinion regarding the merits of such an application.

We also find unfair to Penn Central, for the reasons discussed above, the provision in P&W's charter limiting the voting of more than one-fourth of the outstanding voting stock by a single stockholder. Unless this provision is eliminated by appropriate corporate action by P&W by June 30, 1969, and a one-share one-vote provision adopted, the lease of P&W may, at Penn Central's option, upon notice to P&W's board of directors and this Commission, be terminated as of that date without penalty to Penn Central for such termination. In the event of such termination, P&W's line will be operated by Penn Central without a lease and for the account of P&W.

We direct that, subject to the condition regarding elimination of the voting restriction in P&W's charter, Penn Central operate P&W pursuant to the terms of the lease between P&W and NH and that such lease shall remain in effect until July 1, 1991, or such earlier date as we may prescribe in an appropriate proceeding. We further direct that inclusion of P&W into Penn Central by lease shall be contingent upon and concurrent with the conveyance of NH's properties to Penn Central.

Inclusion of Norwich and Worcester Railroad Company.—The petition of the Norwich and Worcester Railroad Company (Norwich & Worcester) for leave to intervene for the purpose of seeking inclusion in Penn Central in its own right, rather than as part of NH's operation, was denied by order dated July 12, 1965, without prejudice to renewal upon our grant of the Penn Central merger application and inclusion of NH or any part thereof in the merger. The conditions for renewal of its petition having been met, Norwich & Worcester was permitted to intervene for the purpose of seeking inclusion. See our report and order on reconsideration in these

proceedings, 328 I.C.C. 304, 307. A petition for inclusion was filed October 18, 1968. Penn Central has replied.

Like P&W, Norwich & Worcester is a nonoperating lessor of a portion of NH's line of railroad. Its line extends from Worcester, Mass., south to Groton, Conn., a distance of 71.13 miles. It connects with NH, Penn Central and the B&M at Worcester and with NH at Groton. It has been operated under lease by NH since February 9, 1869. The lease expires February 1, 1969. NH owns 1,071 shares of the 30,000 shares of Norwich & Worcester's outstanding stock.[48]

Norwich &Worcester is alleged to provide the only rail service for Auburn, Oxford and Webster in Massachusetts and North Grosvenordale, Grosvenordale, Dayville, Danielson, Wauregan, Central Village, Jewett City, Allyn's Point and Submarine Base in Connecticut. It is purported to be the only connection with NH's line running south to Southbridge, Mass., and if certain portions of NH's line were to be abandoned, as now contemplated, it would remain the only NH connection for Plainfield and the branch line running from Plainfield through Versailles, Baltic, Windham and Willimantic in Connecticut. The petitioner asserts that interline forwarded and received traffic increased by 11.4 percent in freight revenues at stations on its line between 1961 and 1966 and in view of the substantial industrial growth in the area, such increases are expected to continue. The petitioner estimates that the average annual income of its line over the next 10 years to Penn Central before depreciation, income taxes or rental payments would be $2,165,000.

Penn Central requests that we disregard the petitoner's estimates of service, traffic and revenues set forth in the petition. Penn Central argues that evidence is to be presented while the record is still open for its receipt; that the record is now closed; and that the petition is not timely filed. We find and determine that a public hearing is not necessary in the public interest for a resolution of the issues raised in the instant petition and in Penn Central's reply.

In the plan for reorganization of NH adopted elsewhere herein, we affirm the trustees' adoption of Norwich & Worcester's lease. Penn Central has agreed with the petitioner and NH to assume the lease if Penn Central acquires substantially all of NH's

[48]These 30,000 shares, all preferred stock, are each entitled to one vote. There are also 66 shares of common stock outstanding. They were not presented in 1850 for exchange with preferred stock and are presumed to be lost.

property prior to the expiration of the Norwich & Worcester lease on February 1, 1969. In the *merger* report, we required, as a condition to approval of the merger, that the freight and passenger service of NH be included in the merger. The service afforded by NH over the petitioner's line was not excluded from this finding. We have provided in this report for inclusion of NH in Penn Central by January 1, 1969, thus meeting the requirement of Penn Central for assuming the NH lease of Norwich & Worcester. Once assuming the lease, Penn Central may not abandon operations thereunder without our prior authority pursuant to section 1(18) of the act. See *Illinois Central R. Co. Construction and Trackage*, 317 I.C.C. 502, 504. This is true irrespective of whether the petitioner's service traffic and revenue estimates are disregarded as requested by Penn Central. Inasmuch as Norwich & Worcester's line is currently in operation, we may, without making any specific findings as to traffic or revenue, conclude that it is performing a service to shippers that would not be performed if the existence of its line were terminated.

Penn Central contends that upon taking over NH's properties it plans to file an application to abandon operation of the petitioner's line and that we can then fix the terms with respect to the operation even though the lease is terminated. It is not willing to have the terms of the present lease continue after its expiration on February 1, 1969. It requests that Norwich & Worcester's petition for inclusion be denied.

As in the case of P&W, Penn Central is asking us to defer action on Norwich & Worcester's inclusion pending Penn Central's application for authority to abandon the line and, as in the case of P&W, such treatment does not appear justified. Inasmuch as Penn Central is legally required to continue operation of Norwich & Worcester beyond the expiration date of the lease, it does not appear that any undue burden on the Penn Central system would result from continuing the operation under the terms of the present lease until (a) terms of a new lease are arrived at by the parties and approved by us; (b) failing agreement by the parties on terms for a new lease, such terms are prescribed by us; or (c) the line is abandoned pursuant to appropriate authority under section 1(18) of the act. We find that inclusion of Norwich & Worcester in Penn Central, contingent upon and concurrently with inclusion in the latter of NH, is in the public interest and will assure adequate service to the shipping public pending renewal of its lease or whatever other disposition of the company may be found to be in the public interest.

We find that any increase in fixed charges or the assumption or guarantee of payment of dividends or fixed charges resulting from inclusion of P&W and Norwich & Worcester into Penn Central will not be contrary to the public interest. The petition for inclusion of the Boston & Providence Railroad Corporation into Penn Central has been denied in prior reports in these proceedings: 327 I.C.C. 475, 527; 328 I.C.C. 304, 323-324; 331 I.C.C. 754, 763. To the extent, however, that B&P's properties are operated by NH, B&P will be included in Penn Central. 331 I.C.C. 754, 764.

No request has been made for employee protection and it does not appear that any employees of either Norwich & Worcester, the P&W, NH or the Penn Central system will be adversely affected as a result of the inclusion of Norwich & Worcester and P&W. However, for the benefit of any employee of Norwich & Worcester, P&W, NH or the Penn Central system that may be adversely affected as a result of the inclusion of Norwich & Worcester and P&W, we impose the same protective conditions as were prescribed in the *inclusion* report, 331 I.C.C. 643, 728-730.

THE PLAN OF REORGANIZATION

The trustees' reorganization plan provides for the sale of substantially all of NH's assets to Penn Central for the latter's stock, bonds, cash, and assumption by Penn Central of certain NH obligations. After the sale is consummated, Penn Central will conduct NH's railroad operations. The plan further provides for the formation of a reorganized company and the classification and treatment of claims and of the interests of stockholders. One other plan was submitted (the so-called PRIBLIC plan), and it has been rejected as unfeasible. The plan we herein approve is the trustees' plan, modified in certain respects, as hereinafter discussed.

Reorganization plan in general.—The trustees' plan contemplates that after the sale of the NH operating property to Penn Central, NH will be reorganized to carry on business as a closed-end, nondiversified management investment company. The determination whether to reorganize the present NH, or to form a new corporation would be made prior to consummation of the reorganization plan depending on tax considerations, any new legislation pertaining to mergers, and the convenience, simplicity and economy of carrying out either method.

The reorganized company's initial lack of cash would preclude cash distribution to fully satisfy claims against the NH estate, other than current obligations, even though the securities received from Penn Central upon conveyance of the property were to be

sold. The trustees conclude that in fairness to all creditors, the securities should not be sold but that a plan should be formulated to permit the reorganized company to receive and hold those securities intact awaiting achievement of expected benefits from the Penn Central merger, particularly the anticipated further increase in value of the Penn Central stock. Accordingly, the capital structure of the reorganized company and the allotment of equities to claimants and creditors of the NH estate have been designed by the trustees to accomplish this purpose.[49]

Classification of creditor claims and stockholder interests.—Under the trustees' plan the claims of creditors and interests of stockholders are classified into three groups: (1) administration claims, (2) prebankruptcy claims, and (3) interests of stockholders. The approximate amounts of each class of claims in each group as of December 31, 1968, are shown in the table hereunder. Some of the administration claims may be expected to increase somewhat before the effective date of the plan; and the prebankruptcy claims will also increase for unpaid local and State taxes and for the continuing interest on the first mortgage bonds. The three groups of claims are:

Class		Amount
	(1) Administration claims	*Thousands*
A	Costs and expenses of reorganization	$5,000
B	Trustees' certificates	12,500
C	Flood and shop loans	1,747
D	Postbankruptcy taxes and related charges	19,697
E	Postbankruptcy per diem	15,850
F	Other administration claims	10,821
	Total	65,615
	(2) Prebankruptcy claims	
G	Claims of United States	15,335
H	Prebankruptcy taxes and related charges	6,707
I	Harlem River bonds	8,907
J	First mortgage bonds	101,660
K	Income bonds	52,756
L	Equipment obligations	13,181
M	Other claims found by court to be secured	----------
N	General unsecured claims	21,767
	Total	220,313
	(3) Equity interests	
O	Stockholders[1]	48,400

[1]This is the amount recorded on NH's books. However, as indicated later, NH is insolvent and its stockholders have no equity.

[49]See apendixes 4 and 6.

Securities to be assumed or issued by the reorganized company.– The reorganized company will assume or issue under the modified plan three types of debt securities and would issue two kinds of securities related to equity capital. The debt securities to be assumed or issued are (1) trustees' certificates, (2) installment notes, and (3) income notes. The equity securities are (1) 5 million shares of no-par new common stock, and (2) 3 million warrants to purchase new common stock. The number of shares of new common stock and warrants to be issued and outstanding following the confirmation of the plan will be determined by the aggregate amount of the claims at the effective date of the plan for which common stock and warrants are to be issued. The capital structure of the reorganized company, based on assumed consummation dates of December 31, 1968, or December 31, 1970, and excluding Harlem River Division bonds, is as follows:

	December 31, 1968	December 31, 1970
Trustees' certificates	$12,500,000	$12,500,000
Installment notes	5,000,000	5,000,000
Income notes	53,000,000	55,150,000
Total	70,500,000	72,650,000
New common stock–shares	1,536,398	1,536,398
Warrants–number	2,048,710	2,284,228

Description of securities.– The reorganized company will assume or issue the following classes of securities:

1. Trustees' certificates: The maturity of certificates outstanding at the effective date will be extended to a date 7 years from the court's order confirming the plan, or to such subsequent date as may be fixed by the court, and the interest rate will be modified.

2. Installment notes: Each note will bear the date of its issuance and will mature in five equal annual installments commencing with the first anniversary of its date of issuance. These notes will not bear interest.

3. Income notes: Each note will mature 7 years from the confirmation date of the plan and bear interest at the rate of 5 percent per annum which, to the extent unpaid, will be cumulative. Payment of interest will be contingent upon the availability of adjusted net income as defined in the plan. The income notes will be subordinated in right of payment to the installment notes and

trustees' certificates. Payment of interest on, and retirement of, the income notes will be permitted so long as there is no default in any obligation of the reorganized company to which the income notes are subordinated.

4. New common stock: Each share of new common stock will entitle the holder to one vote. The voting rights will not be cumulated. The holders of this stock will not have preemptive rights.

5. Warrants: Each warrant will entitle the holder to purchase one share of new common stock for $50 at any time during the 10 years succeeding the confirmation date of the reorganization.

Effect of the plan on stockholders.—This discussion gives effect to the acquisition by NH of the properties of the B&P, the purchase agreement between NH and Penn Central, and the approved plan of reorganization.

Class A-costs and expenses of reorganization.—The claims in this class are represented by the anticipated final allowances under sections 77(c)(2) and 77(c)(12) of the Bankruptcy Act for fees and expenses incurred in connection with completion of the reorganization proceedings and consummation of the plan. As estimated by the trustees, they will not exceed $5 million, an amount we accept for illustration. They will be paid as detailed later either in cash or installment notes equal in principal to the claims at the effective date of the reorganization or at times we and the reorganization court may fix.

Class B-trustees' certificates.—There are $12.5 million in trustees' certificates outstanding which bear interest at the rate of 5 1/4 percent per annum. Of the principal amount, $5 million mature on August 4, 1971, and $7.5 million on December 31, 1971.

The plan will extend the maturity of the certificates to a date 7 years from the confirmation date of the reorganization. The interest rate will be changed to the prime rate of the Morgan Guaranty Trust Company of New York City as of the said confirmation date, but not less than 5 1/4 percent per annum. A sinking fund will be established commencing with the fourth anniversary of the confirmation date to retire annually 10 percent of the principal amount outstanding at the effective date of the plan. As a result, about 30 percent of the principal amount of these trustees' certificates will be retired prior to the new maturity date, if we assume confirmation as of December 31, 1970.

Class C-flood and shop loans.—The claims of this class (originally $4.5 million) are owed to the United States in respect

to flood and shop loans. The plan contemplates that approximately $1.7 million of these claims will be paid in cash. To the extent that claims (current balance of $2.8 million) are not paid in cash, they will be represented by the proposed B&P bonds which will be assumed by Penn Central.

Class D-taxes commencing July 7, 1961.–The amount of taxes and related charges assessed by State and local authorities is for the period beginning July 7, 1961, and amount unpaid is about $19.7 million. Such taxes and charges continue to accrue at the rate of $2.5 million a year. In the amount to be determined by the reorganization court, they will be paid by an equal amount of income notes. No payment will be made for interest applicable to such period or for any penalty or other such charge.

Class E-freight car rentals beginning July 7, 1961.–The per diem claims against NH are in dispute. The amount applicable to the period commencing July 7, 1961, is about $15.9 million. The claims for car rentals accrue at the rate of $2.2 million a year. The trustees propose to pay the amount of the per diem claims as determined in appropriate proceedings, or as settled from time to time by the trustees or the reorganized company with the claimants, by the issuance and delivery of an equivalent amount of income notes.

Class F-other administration claims.–This class consists of claims, other than classes A through E, of administration expenses found by the reorganization court to be entitled to treatment as administration claims. NH's books show some $11 million in personal injury and property damage claims and reserves related thereto. The trustees estimate that approximately $5.8 million will be recognized by the reorganization court as claims of administration. In addition there are some $26.8 million in general unsecured claims apart from claims of the United States. Of that total, approximately $4.7 million are for liabilities incurred within 6 months of the date NH petitioned for reorganization.[50] The trustees estimate that claims for $5 million will receive treatment as administration expenses under the reorganization plan. Thus, the total amount estimated by the trustees in class F is $10.8 million. Class F claims will be paid by issuance and delivery of income notes in principal amount equal to that determined by the reorganization court.

[50] The reorganization court has held that no preferential treatment would be afforded the 6-months claim (chiefly representing claims for goods and services rendered to the debtor during the 6 months prior to filing the petition in reorganization) but appeals have been taken.

Class G-claims of the United States.—These are unsecured claims of the United States other than class C, and total approximately $15.3 million. None of these represents taxes or custom duties referred to in section 77(e) and since they are unsecured, they have no value. These claims have no value; they will be treated as class N claims and will not be paid.

Class H-taxes due prior to July 7, 1961.—These claims of States and local authorities for taxes and related charges due prior to July 7, 1961, and unpaid, total approximately $6.6 million on NH's books. In addition, there is approximately $100,000 unpaid interest on such taxes. Under the plan, claims for taxes and interest in the amount determined by the reorganization court, will be satisfied with income notes of an equivalent amount.

Class I-Harlem River bonds.—Harlem River bonds are outstanding in the principal amount of $6.6 million. Accrued unpaid interest on these bonds is about $2.3 million, making approximately $8.9 million payable to their holders. Interest accrues at the rate of 4 1/4 percent per annum. The principal amount of the Harlem River bonds and the accrued interest will be assumed by Penn Central subject to the modifications we have already discussed.

Class J-first mortgage bonds.—The principal amount of first mortgage bonds outstanding is $76.8 million. Accrued unpaid interest on these bonds amounts to about $24.8 million, as of December 31, 1968, making approximately $101.6 million payable to their holders. Interest accrues at the rate of 4 percent per annum. Payment of the principal amount will be in new common stock at the rate of one share of such stock for each $50 of principal outstanding at the effective date. Interest accrued will be paid through issuance and delivery of one warrant for each $25 of accrued interest. Scrip for warrants will be issued in lieu of fractional warrants.

Class K-income bonds.—There are $52.8 million in income bonds outstanding. Accrued and unpaid contingent interest on these bonds totals $7.1 million. The income bonds will be paid by one warrant for each $50 principal amount of the bonds outstanding at the effective date of the reorganization. Scrip will be issued in lieu of fractional warrants. Contingent interest will not be paid.

Class L-equipment obligations.—These obligations, $13.2 million, will be assumed by Penn Central pursuant to agreement with the trustees. Any equipment obligations not so assumed are rejected, and claims arising thereunder will not be paid.

Class M-other prebankruptcy claims found by the court to be secured.– The trustees provided this class as a catchall for any claims which were applicable to the period prior to July 7, 1961, other than those specifically included in classes H through L, which might be found by the reorganization court to be secured. However, while the trustees know of no claims which would be included in this class, they believe that a class of this nature is desirable to cover contingencies. Such claims, if any, are to be paid by the issuance of income notes in principal amount thereof, plus interest to July 7, 1961, as may be determined by the reorganization court.

Class N-general unsecured claims.–General unsecured claims, including 6-month claims, other than claims of the United States in class G, total some $21.8 million, apart from the $5 million to be treated as administration claims in class F. The major items are $10.8 million in claims for freight car rental applicable to the period prior to July 7, 1961, and the $7.1 million in accrued and unpaid contingent interest on the income bonds. Class N claims have no value and no payments will be made on such claims.

Class O-equity interests.–NH has 539,830 shares of no-par value common stock oustanding recorded on its books at $53.9 million, and 491,263 shares of $100 par value preferred stock at $49.1 million. In addition, there are 534,038 shares of undistributed common and 277 shares of preferred at $53.5 million, a total of $156.5 million for stock. The total shareholders' equity is recorded at $156.5 million for stock less accumulated deficit of $108.1 million, or a net equity of $48.4 million. Since the debtor is insolvent and the equity of its stockholders has no value, no provision is made in the plan for any payment to shareholders. Accordingly, we find that submission of the plan to NH stockholders shall not be necessary.

Financial condition and requirements of reorganized company.– On the assumption that the reorganization might not be consummated until December 31, 1970, the balance sheet, excluding current items, of the reorganized company at the time of consummation would be substantially as follows:

Assets	*Thousands*
Penn Central stock	$83,125
Penn Central bonds	33,600
Total	116,725

Liabilities and capital	*Thousands*
Trustees' certificates	$12,500
Installment notes	5,000
Income notes	55,150
Total liabilities	72,650
Capital stock	44,075
Total	116,725

The 950,000 shares of common stock to be received from Penn Central are valued at $87.50 per share. However, in the opinion of the trustees, some 7 to 10 years after consummation of the plan of reorganization, the Penn Central stock might well have a value in excess of $144 per share and possibly even in excess of $150 per share.

The trustees anticipate that over a period of years the dividends on the Penn Central stock and proceeds from bonds will meet the requirements for payment of interest and sinking fund as well as the estimated $100,000 annual operating expenses for the reorganized company. See appendix 5.

The trustees further believe that the reorganized company will have sufficient cash available through the first 6 years of its existence to meet its obligations. The provision that interest on the income notes be contingent rather than fixed provides a safeguard for the reorganized company during the early years of its existence. If the value the trustees have estimated for the Penn Central stock will have materialized by the 7th year, the trustees believe the reorganized company can make appropriate arrangements to meet its maturing debt, either through borrowing, other refinancing or a sale of assets. We agree with the trustees that their plan, as modified herein, is feasible and fair to all creditors.

Bondholder interests.—The NH trustees believe that each warrant issued to income bondholders will have a market value of about $5 upon issuance. However, the value of the common stock of the reorganized company would not be diluted prior to the time its market value reached at least $50 per share. At that time, the holder of a warrant could obtain a share of common stock through exercise of his warrant and payment of $50 into the treasury of the reorganized company. Thus, the attainment of such market value in the stock would demonstrate value in the warrants. Moreover, the exercise of warrants would provide cash for the reorganized company and thereby increase the asset value supporting the debt securities.

If the common stock of the reorganized company does not reach a value of $50 per share before the expiration of the 10-year life of the warrants and the rights are not exercised, the interests of the senior securities will not be adversely affected. On the other hand, participation of income bondholders in the estate, by issuance of 10-year warrants, in recognition of value based on expected increase in market value of Penn Central holdings (see appendix 6), will safeguard their equity and avoid undue benefits to the other creditors of the estate.

In view of the savings from the Penn Central merger and the potential increase in value of Penn Central stock, we find that recognition of the income bondholders' equity in the NH estate is fair and equitable. We find further that recognition of such equity is fairly provided for in the trustees' plan by provision for issuance of the 10-year warrants for the principal amount of income bonds with no provision for accrued interest.

The holders of the First and Refunding Mortgage bonds request that common stock, instead of warrants, be issued for accrued interest. The accrued interest claims of these bondholders is recognized in the plan by warrants for purchase of stock at the rate of one warrant for each $25 of accrued interest. Having recognized the equity of the junior income bondholders by provision for issuance of warrants for each $50 of bond principal (and extinguishing accrued interest), the prior claim of the first and refunding bondholders for accrued interest is provided for by provision for issuance of warrants to these senior bonds by granting rights worth twice as much, per dollars of claim, as rights granted to the income bondholders for *principal*. In the circumstances, this is fair and equitable treatment for the first and refunding bondholders' claim for accrued interest. Their request for issuance of common stock, instead of the warrants provided for in the plan, is denied.

Postbankruptcy interest on prebankruptcy taxes.—With regard to the matter of postbankruptcy interest on prebankruptcy taxes, which creditors contend should not be paid, the trustees indicate it would be appropriate to pay such interest to the effective date of the plan. The plan requires that these claims to the effective date shall be paid by income notes if found by the reorganization court to be secured.

The reorganized investment company.—The trustees have proposed the continuance of NH as an investment company which would be subject to the Investment Company Act of 1940, and,

thereby, to regulation by the Securities and Exchange Commission. This proposal raises several questions concerning our jurisdiction and the general conformity of the trustees' proposal with the Investment Company Act respecting the election of directors, asset coverage of debt and limitations on the issuance of securities and warrants.[51] None of the creditors or other parties involved herein contend that we lack jurisdiction over the reorganization proceeding solely on the ground that the resulting corporation will be an investment company rather than a common carrier subject to our regulation under the Interstate Commerce Act.

Section 77 of the Bankruptcy Act authorizes a railroad to file a petition in the Federal district court in whose territorial jurisdiction it has its principal executive or operating office, stating that it is insolvent or unable to meet its debts as they mature, and that it desires to effect a plan of reorganization. At the same time, the carrier is required to file a copy of the petition with this Commission. If the court is of the opinion that the petition is properly filed, it enters an order approving the petition. Within 6 months after approval of the petition, the carrier is required to file its plan with the court and to serve a copy thereof upon this Commission. At that time our jurisdiction attaches over various phases of the proposed reorganization plan and we become the chief architect of the plan. *St. Joe Paper Co.* v. *Atlantic Coast Line R. R.*, 347 U.S. at 322. We are directed by section 77 to hold hearings on the plan and then to approve the plan as proposed or to make such modifications therein as we deem desirable and necessary. In the language of the Supreme Court, Congress delegated to "the [Interstate Commerce] Commission the primary responsibility for the development of a suitable plan" and placed "reorganization under the leadership of the Commission * * *" *Ecker* v. *Western Pacific R. Corp.*, 318 U. S. 448, 468 (1943).

The act does not require a carrier to continue in common carriage following reorganization. Neither does it prohibit the creation of a noncarrier corporation. In fact, section 77(b)(5) author-

[51] It appears that the trustees' reorganization plan with respect to the creation of an investment company, may fail to meet the requirements of the Investment Company Act in four areas: (1) the Investment Company Act requirement for 300 percent asset coverage of debt securities; (2) the limitation with respect to securities issued (the reorganization plan provides for four classes); (3) restriction on issuance of warrants; and (4) requirement that the Board of Directors be elected annually by the holders of voting securities—no provision being made for court-appointed directors in the Investment Company Act as specified in the trustees' plan.

izes the formation of another corporation and the issuance of securities by such corporation. Moreover, section 77(b)(5) requires that the plan "shall provide adequate means for the execution of the plan," including the transfer of any interest or control of the debtor to another corporation or corporations. Here, the debtor's assets will be conveyed to two corporations. Virtually all of the railroad properties of NH will be transferred to Penn Central, and the consideration therefrom in the form of assets will be transferred to the reorganized company along with the retained assets. In specifying the methods of effectuating a plan of reorganization, section 77(b)(5) includes several permissible alternatives, including, among others, the issuance of securities by the debtor or by "any such other corporation" and "any other appropriate provisions not inconsistent with this section."

In our view, the formation of an investment company, which is necessary and incident to the effectuation of the trustees' plan, is fully consistent with section 77(b)(5) and with all other provisions of the Bankruptcy Act. One of the main purposes of the Bankruptcy Act is to permit creditors to share in the assets of the debtor, and the statutory methods of accomplishing that objective, including several specific methods and "other appropriate provisions," are relatively flexible. Thus, in order to carry out the intent of Congress, it would appear that a corporation not engaged in the railroad business may emerge from the reorganization as a convenient and necessary device for effectuating the overall plan. The trustees' plan merely amounts to the postponement of the distribution of proceeds derived from the sale of the debtors' assets and the substitution of another corporation to assume or satisfy the debtors' obligations. There is no prohibition in the act against this approach. In the circumstances here, we believe that the creation of an investment company and the issuance of securities by it in exchange for the debtor's securities provide the most feasible means for effectuating the plan, and that such method is consistent with congressional intent as well as the language of section 77.

Undoubtedly, we have jurisdiction over the debtor under section 77 and once jurisdiction has attached, our jurisdiction continues until the problems which led to NH's initial petition under section 77 have been resolved. Accordingly, we will retain jurisdiction over the entire matter until the reorganization of the debtor is completed. To do otherwise would force the trustees to seek completion of their plan under chapter X of the Bankruptcy Act

(11 U. S. C., sec. 506) in a wholly unrelated proceeding. Section 77 is designed to alleviate the expense and delay inherent in reorganization through equity receivership. Another reorganization proceeding under chapter X would, in effect, constitute an ancillary proceeding to the present reorganization, which would thereby recreate and perpetuate the deficiencies of equity receivership proceedings. Obviously, such multiple procedures would defeat the purposes and objectives of section 77. In our opinion it is our responsibility to pursue to finality the proceeding instituted by NH since the statute specifically requires that no plan shall be approved or confirmed by the court in any proceedings unless the plan shall have first been approved by us and certified to the court. See *Ecker* v. *Western Pacific R. Corp., supra.* We believe that the language of section 77 is sufficiently flexible to enable us to retain jurisdiction over NH's plan of reorganization notwithstanding the transfer of railroad operations to a different carrier and the formation of a noncarrier investment company.

The trustees believe that the appropriate time to seek formal ruling from the Securities and Exchange Commission for exemptions under the Investment Company Act should be sometime prior to submission of the plan for acceptance or rejection by those persons entitled to vote on the plan. They consider, however, that in the present stage of the reorganization proceeding, this Commission should assume that appropriate exemptions will be forthcoming from the Securities and Exchange Commission to enable consummation of the trustees' plan. The Securities and Exchange Commission has informally indicated that it would not oppose the granting of the exemptions.

The creditors take different positions on the initial organization of the company, and its first group of directors. The management of the reorganized company is of major importance, particularly during its early years. The trustees maintain that the interests of the board of directors in the early years should not stem from any particular class of securities. To accomplish this objective, the plan provides that the reorganization court should appoint the first board. The trustees propose that the board should be small—five members—and the terms of the initial members should be staggered up to 5 years so as to provide continuity in the management of the reorganized company. We agree with the trustees on this aspect of the plan.

We approve the trustees' plan for creation of an investment company and we agree with the proposal to seek a formal ruling

from the Securities and Exchange Commission for necessary exemptions from the Investment Company Act of 1940.

ULTIMATE FINDINGS

We conclude and find:

(a) That as modified herein, the *inclusion* report and order and the *third supplemental* report and order are reinstated and affirmed;

(b) That the inclusion in the Penn Central system of the Providence and Worcester Railroad Company and the Norwich and Worcester Railroad Company upon the terms and conditions found herein to be in the public interest, are transactions within the scope of section 5(2) of the act;

(c) That the issuance by the Penn Central Company of $33,600,000 principal amount of 25-year Divisional First Mortgage bonds and such larger amount of bonds as may result from operation of the purchase price adjustment provisions herein is for lawful objects within the corporate purposes of the Penn Central Company, compatible with the public interest, which are necessary and appropriate for and consistent with the proper performance by it of service to the public as a common carrier, and will not impair its ability to perform that service; and reasonably necessary and appropriate for such purpose;

(d) That The New York, New Haven and Hartford Railroad Company, debtor, is insolvent within the meaning of section 77(e) of the Bankruptcy Act;

(e) That the plan of reorganization as herein described meets the requirements of section 77(b) of the Bankruptcy Act; and

(f) That the terms and provisions of the plan are fair and equitable, afford due recognition to the rights of each class of creditors and stockholders, and do not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders and will meet the requirements of subsection (e) of section 77 and will be compatible with the public interest.

An appropriate order incorporating by reference the plan of reorganization will be entered.

The approved plan of reorganization follows:

PLAN OF REORGANIZATION

SECTION I

Definitions

For purposes hereof, the following terms shall have the meanings set forth, unless a different meaning in a specific instance is clearly required by the context.

1. Inclusion report —the second supplemental report and orders decided November 16, 1967, 331 I.C.C. 643.

2. Bankruptcy Act —the Bankruptcy Statute of 1898 as amended to the date of any reference made thereto in connection with this plan.

3. Commission —Interstate Commerce Commission.

4. Court—the United States District Court for the District of Connecticut having jurisdiction in the reorganization proceedings of the debtor.

5. Debtor —The New York, New Haven and Hartford Railroad Company, a corporation organized under the laws of Connecticut, Massachusetts and Rhode Island, in reorganization under section 77 of the Bankruptcy Act in the court, docket No. 30226.

6. Plan —this plan filed pursuant to section 77(d) of the Bankruptcy Act with the court in docket No. 30226 and with the Commission in Finance Docket No. 21669 by Richard Joyce Smith and William J. Kirk, trustees, in the form filed or as amended, modified or supplemented by the trustees, or the Commission.

7. Stockholders —all holders of preferred stock, common stock or certificates of beneficial interest of the debtor.

8. Trustees —Richard Joyce Smith and William J. Kirk, as trustees, and not individually, of the property of the debtor or any person or persons appointed or continued by the court as trustee, or as successor or successors to or in substitution for them or either of them.

9. Reorganized company —the corporation, whether the debtor or a new corporation formed as provided in the plan, which is vested with the assets of the debtor, including the proceeds of the sale of the debtor's assets pursuant to the *inclusion* report, and which is the issuer of an obligor under the securities to be issued and assumed as provided by the plan.

10. Effective date —the date of the Commission's order, as provided in section 77(d) of the Bankruptcy Act, approving the plan, thereafter certified to the court.

11. Confirmation date.—the date of the court's order, as provided in section 77(e) of the Bankruptcy Act, confirming the plan, unless consummation of the plan shall have been stayed, in which event, the confirmation date shall be such subsequent date as may be fixed by the court.

12. Consummation of the plan —the carrying out of all acts and procedures contemplated by the plan commencing with the confirmation date. The consummation date shall be the date on which the court shall have entered a final decree closing the case, as provided in section 77(e) of the Bankruptcy Act.

13. Harlem River bonds.—the bonds issued under and secured by the lien of debtor's Harlem River Division Indenture of First Mortgage, dated as of January 1, 1953, from the debtor to United States Trust Company of New York, trustee, maturing January 1, 1973, and bearing interest at the rate of 4 1/2 percent per annum.

14. First mortgage bonds —the bonds issued under and secured by the lien of the debtor's first and refunding mortgage, dated as of July 1, 1947, from the debtor to Manufacturers Hanover Trust Company, trustee, maturing July 1, 2007, and bearing interest at the rate of 4 percent per annum.

15. Income bonds —the bonds issued under and secured by the lien of the debtor's general income mortgage, dated as of July 1, 1947, from the debtor to The Chase Manhattan Bank, N. A., trustee, maturing July 1, 2022, and bearing interest at the rate of 4 1/2 percent per annum.

16. Trustees' certificates —the debt instruments issued by the trustees in accordance with orders of the court to Irving Trust Company, dated August 4, 1961 and maturing August 4, 1971, and dated December 13, 1961 and March 4, 1965, respectively, and maturing December 13, 1971, each such instrument bearing interest at the rate of 5 1/4 percent per annum.

17. Installment notes —the debt instruments of the reorganized company described in section IV 2 of the plan.

18. Income notes —the debt instruments of the reorganized company described in section IV 3 of the plan.

19. Equipment obligations —claims secured by liens or other encumbrances in respect of the equipment obligations, purchase order agreements, equipment trusts, conditional sale contracts and equipment leases described in account No. 763, account No. 764, account No. 766, and account No. 782, maintained in accordance with the Uniform System of Accounts for Railroad Companies Prescribed by the Interstate Commerce Commission, as shown by the books of the debtor.

20. New common stock —the common stock of the reorganized company described in section IV 5 of the plan.

21. Warrants —the warrants of the reorganized company described in section IV 6 of the plan.

22. Claims —claims as defined in section 77(b) of the Bankruptcy Act.

23. Six-months claims —all claims to which preferential treatment, as 6-months creditors' claims, is asserted.

24. Administration claims —all claims arising on or after July 7, 1961, or applicable to a period commencing on and after such date, which are found by the court to be entitled to priority by classification in classes A, B, C, D, E and F of the plan.

25. Flood and shop loans—claims of the United States being discharged in accordance with order No. 347, dated December 30, 1965, of the court as modified.

SECTION II

Classification of Creditor Claims and Stockholder Interests

For the purposes of the plan, the classification of claims and of the interests of stockholders is as follows.

1. *Administration claims.*

Class A.—Costs and expenses incurred in connection with the reorganization proceedings and the plan, as may be fixed by the Commission and allowed by the court in accordance with the provisions of sections 77(c)(2) and 77(c)(12) of the Bankruptcy Act.

Class B.—Trustees' certificates.

Class C.—Flood and shop loans.

Class D.—Claims of State and local authorities for taxes and related charges applicable to the period commencing July 7, 1961.

Class E.—Claims for freight car rentals applicable to the period commencing July 7, 1961.

Class F.—Claims, other than those in classes A through E, found by the court to be entitled to be treated as administration claims.

2. *Prebankruptcy claims.*

Class G.—Claims of the United States other than those in class C.

Class H.—Claims of State and local authorities for taxes and related charges applicable to the period prior to July 7, 1961, found by the court to be secured.

Class I.–Harlem River bonds.

Class J.–First mortgage bonds.

Class K.–Income bonds.

Class L.–Equipment obligations.

Class M.– Claims applicable to the period prior to July 7, 1961, other than those in classes H through L, found by the court to be secured.

Class N.–General unsecured claims, including 6-month claims, other than those in class G.

3. *Interests of stockholders.*

Class O.– Interests arising from ownership of preferred stock, common stock and certificates of beneficial interest of the debtor.

4. *Effect of plan on claims.*

(a) Class C is not adversely affected by the plan because the claims in such class will be satisfied in accordance with order No. 347 of the court;

(b) Class G is affected by the plan, but shall be treated as class N claims;

(c) Class I is not adversely and materially affected by the plan, since these claims will be assumed by Penn Central pursuant to the present report and order;

(d) Class L is not affected by the plan because the claims in such class will be assumed by Penn Central or rejected by the trustees;

(e) Class N is affected by the plan, but the plan should not be submitted to such class for acceptance or rejection because the debtor's assets are insufficient to pay any part of these claims, and hence they are without value;

(f) Class O is affected by the plan, but the plan should not be submitted to any interests in such class for acceptance or rejection because the debtor is insolvent; and

(g) All other classes are affected by the plan, and the plan should be submitted to such classes for acceptance or rejection, either before or after transfer of the assets to Penn Central pursuant to the instant report.

SECTION III

Creation of the Reorganized Company

The reorganization of the debtor shall be effected as follows: Essentially all of its operating assets shall be transferred as pro-

vided in the instant report, and, as soon as practicable, new securities of the reorganized company shall be distributed in full satisfaction and discharge of all claims in the debtor's estate.

The reorganized company shall carry on business as an investment company. The determination whether to continue the existence of the debtor with a capital structure revised as provided by the plan and appropriate articles of incorporation and bylaws, or to form a new corporation having such capital structure, and articles and bylaws, shall be made prior to consummation of the plan. The basis for such determination shall be the then applicable tax considerations and convenience, simplicity and economy in carrying out the plan.

1. *Conveyance of assets to Penn Central.*—As soon as practicable after entry by the reorganization court of an order authorizing such a transfer, the assets of the debtor will be conveyed to Penn Central pursuant to the terms and conditions of the *inclusion* report as modified by the instant report. The consideration received from Penn Central shall be vested in the debtor and transferred to the reorganized company.

The liens, charges and encumbrances to which the debtor's assets were subject immediately prior to the conveyance of such assets pursuant to the instant report shall be recognized as continuing liens, charges and encumbrances upon the assets thereafter held by the debtor. Such liens, charges and encumbrances shall be in such order and of such rank with respect to the assets of the debtor as they were immediately prior to the conveyance of the assets of the debtor impressed with such lien, charge or encumbrance. Any lien, charge or encumbrance having a claim on a specific asset shall have priority in an amount equal to the fair market value as of the date of conveyance of the assets to which such lien, charge or encumbrance applied immediately prior to such conveyance.

2. *Capitalization of the reorganized company.*—The equity capitalization of the reorganized company shall consist of 5 million shares of new common stock and 3 million warrants to purchase new common stock. The number of shares of new common stock and warrants to be issued and outstanding following the confirmation date is to be determined by the aggregate amount of the claims at the effective date for which shares of new common stock and warrants are required to be issued as herein provided. In addition to its new common stock and warrants, the reorganized company shall assume the trustees' certificates and shall issue installment notes and income notes.

The maximum principal amount of installment notes and income notes to be issued in consummation of the plan shall be determined by the aggregate amount of the claims, for which such issuances will be made as herein provided, at the effective date or, where such maximum amount is not then known, as thereafter fixed by order of the court.

3. *Assets of the reorganized company.*– In addition to the consideration received from Penn Central, the reorganized company shall be vested with all other assets and claims of the debtor as they become available. All cash or other property under instruments securing obligations of the debtor, all collateral securing obligations of the debtor, and all segregated or special deposits or funds of any type held by the debtor, by the trustees, by any indenture trustee, by any other person, or in the registry of the court shall be delivered to the reorganized company as soon as practicable after the confirmation date, except as provided in the instant report or any order of the court. See appendix 7.

4. *Obligations of the reorganized company.*– All obligations of the trustees outstanding following the confirmation date, or thereafter incurred by the trustees shall be assumed by the reorganized company. The reorganized company shall indemnify the trustees and their agents and attorneys, the officers of the debtor acting under direction of the trustees, any indenture trustee, depositary or distribution agent under the plan, the trustees under instruments securing obligations of the debtor, any transfer agent, registrar or scrip agent for the new common stock and warrants, and such other persons as may be ordered by the court, against all losses, costs, liabilities and expenses resulting from any transaction required or authorized by the plan, subject, however, to any order of the court in the premises. The reorganized company shall assume all obligations of the debtor for which payment is provided by the plan.

5. *Business of the reorganized company.*– The reorganized company shall register pursuant to the Investment Company Act of 1940 as a closed-end, nondiversified, management investment company, and shall seek such exemptions under said act as may be necessary in view of its capital structure or otherwise. The investment policy of the reorganized company shall be such as may be approved by the Commission and the court as necessary and appropriate.

SECTION IV

Securities to be issued by the reorganized company

The securities to be assumed or issued by the reorganized company in carrying out the plan shall have the specific terms and forms as may be later approved by this Commission and the court as being appropriate, and shall have the following general terms and provisions:

1. *Trustees' certificates.*—The maturity of the trustees' certificates outstanding at the effective date shall be extended to a date 7 years from the confirmation date. The interest rate shall be changed to the prime rate of the Morgan Guaranty Trust Company of New York City as of the said confirmation date, but not less than 5 1/4 percent per annum. A sinking fund shall be established commencing with the fourth anniversary of the confirmation date to retire annually 10 percent of the principal amount outstanding at the effective date.

2. *Installment notes.*—Each installment note shall be dated the date of its issuance and mature in five equal annual installments commencing with the first anniversary of its date of issuance. The installment notes shall not bear interest.

3. *Income notes.*—Each income note shall mature 7 years from the confirmation date and bear interest at the rate of 5 percent per annum, which to the extent unpaid shall be cumulative. The payment of interest shall be contingent upon the availability of adjusted net income for the payment of such interest. Adjusted net income shall be defined in the income notes as being the income of the reorganized company determined in accordance with generally accepted accounting principles, after deduction of interest and sinking fund payments on the trustees' certificates and all payments required to be made on the installment notes. The income notes will be subordinated in right of payment to the installment notes and trustees' certificates; but payment of interest on, and retirement of, income notes shall be permitted so long as there is no default in any obligation of the reorganized company to which the income notes are subordinated.

4. *New common stock.*—Each share of new common stock shall entitle the holder thereof to one vote at all meetings of stockholders. Such voting rights shall not be cumulative. The holders of new common stock shall not have preemptive rights. The new common stock shall have no par value.

5. *Warrants.*–Each warrant shall entitle the holder thereof to purchase one share of new common stock for $50 at any time during the 10 years next following the confirmation date. The warrants shall contain an appropriate provision against dilution in the event of issuance for cash of new common stock at a price less than $50 per share.

SECTION V

Treatment of creditor claims and stockholder interests

The treatment of claims and other interests shall be as follows.

1. *Administration claims.*

Class A.–Payment of expenses and allowances, as distinguished from fees, shall be made in cash. Fees shall be paid by issuance and delivery of installment notes equal in principal to the claims at the effective date or as thereafter fixed from time to time by orders of the Commission and the court.

Class B.–Trustees' certificates shall be extended in maturity with modified interest rate.

Class C.–Flood and shop loan claims shall be satisfied in accordance with order No. 347 of the court, as modified.

Class D.–Claims of State and local authorities for taxes and related charges applicable to the period commencing July 7, 1961, shall be paid by issuance and delivery of income notes in principal amount equal to the principal amount of the claims as may be determined by the court. No payment will be made for interest applicable to such period or for any penalty or other such charge.

Class E.–Claims for freight car rentals applicable to the period commencing July 7, 1961, shall be paid by issuance and delivery of income notes in principal amount equal to the principal amount of the claims as may be finally determined in appropriate proceedings, or as may be settled from time to time by the trustees or the reorganized company with the claimants.

Class F.–Claims, other than those in classes A through E, which may be found by the court to be entitled to be treated as administration claims, shall be paid by issuance and delivery of income notes in principal amount equal to the principal amount of the claims as may be determined by the court.

2. *Prebankruptcy claims.*

Class G.–Claims of the United States, other than those in class C, shall be treated as class N claims, referred to below.

Class H.—Claims of State and local authorities for taxes and related charges applicable to the period prior to July 7, 1961, that may be found by the court to be secured, together with the interest accrued thereon to July 7, 1961, if found by the court to be secured, shall be paid by issuance and delivery of income notes in principal amount equal to the amount of the claims as may be determined by the court. Claims for postbankruptcy interest, if found by the court to be secured, shall be paid by income notes in principal amount equal to the amount of the claims, in the same manner as interest to July 7, 1961. No payment is to be made for any penalty or other such charge.

Class I.—Harlem River bonds shall not be paid by the estate, since they will have been assumed by Penn Central pursuant to the order of the Commission.

Class J.—First and refunding mortgage bonds shall be paid by issuance and delivery of one share of new common stock for each $50 principal amount outstanding at the effective date. All interest accrued on the first mortgage bonds to the effective date shall be paid through the issuance and delivery of one warrant for each $25 of accrued interest. Scrip for warrants shall be issued in lieu of factional warrants.

Class K.—Income bonds shall be paid by issuance and delivery of one warrant for each $50 principal amount outstanding at the effective date. No payment shall be made for any interest accrued on the income bonds. Scrip for warrants shall be issued in lieu of fractional warrants.

Class L.—Equipment obligations are to be assumed by Penn Central pursuant to the order of the Commission. Any equipment obligations not so assumed shall be rejected by the trustees, and claims arising thereunder shall be treated as class N claims.

Class M.—Claims applicable to the period prior to July 7, 1961, other than those in classes H through L, which may be found by the court to be secured, shall be paid by the issuance of income notes in principal amount of the claims, plus interest to July 7, 1961, as may be determined by the court.

Class N.—General unsecured claims, including 6-month claims, except as otherwise indicated herein, shall not be paid.

3. *Interests of stockholders.*

Class O.—No provision shall be made for participation in the assets by the stockholders. . .

SECTION VI

Executory contracts

1. The debtor's adoption of the leases with Norwich & Worcester Railroad Company and Holyoke and Westfield Railroad Company is affirmed. The lease with Providence and Worcester Railroad Company, dated December 17, 1892, as amended, is rejected, in accordance with the provisions of section 77(b) of the Bankruptcy Act, and will be assumed by Penn Central pursuant to order of the Commission.

2. In accordance with the provisions of section 77(b) of the Bankruptcy Act, the following executory contracts of the debtor are rejected:

(1) a lease, dated December 7, 1869, recorded in the Berkshire County Registry of Deeds, Great Barrington, Mass., in book 131 at page 547, from William and Jane Bates to the Housatonic Rail Road Corporation (merged with the debtor in 1898) covering the right to maintain a locomotive watering facility at Ashley Falls in the town of Sheffield, Mass.;

(2) a lease, dated as of October 21, 1954, amended as of December 13, 1957, from Kitty Freeman Jacobs, et al. (as assignees of Providence Produce Warehouse Company, Inc.) relating to land and buildings at 1080 Leggett Avenue, Bronx, N. Y.;

(3) a sublease, dated as of December 23, 1959, between the debtor, as lessor, and The Borden Company, as lessee, relating to land and buildings at 1080 Leggett Avenue, Bronx, N. Y.;

(4) a joint facility agreement with the Boston and Maine Railroad Company, dated April 14, 1950, as amended, relating to railroad facilities in Springfield, Mass.; and

(5) three leases (bareboat charters), dated July 1, July 15, and September 9, 1957, respectively, from Dalzell Harbor Corporation (now known as Lacey Harbor Corporation) relating to the tugs "Dalzell 1," "Dalzell 2," and "Dalzell 3," respectively.

3. Other executory contracts or agreements of the debtor may be rejected by amendment to this plan, subject to the provisions of section 77 of the Bankruptcy Act and all requisite approvals.

SECTION VII

Reservation of claims

All claims in favor of the debtor not settled or determined by the plan or during consummation of the plan shall be assumed and enforced by the reorganized company in such manner as the court shall determine. The defense of all claims against the debtor or the trustees which have not been finally allowed or disallowed prior to the confirmation date shall be assumed and defended by the reorganized company in such manner as the court shall determine. The reorganized company shall have power, subject to the approval of the court and, where applicable, the Commission, to employ, retain or replace attorneys and other experts to prosecute or defend any action or proceeding involving the debtor or the trustees. The obligations or proceeds resulting from any such action or claim shall be received or paid pursuant to the plan. For purposes of such actions or claims, the court shall retain jurisdiction over the trustees, the debtor and the reorganized company and their respective books, records and papers, until final decree.

SECTION VIII

Claims undetermined prior to the confirmation date

Any claim against the debtor in a class entitled to participate under the plan but which was not finally settled or adjudicated prior to the confirmation date and which shall thereafter be adjudicated to be valid, or which shall otherwise be determined, or which shall be settled, shall participate under the plan as determined by the court. For the purposes of adjudication, determination or settlement of any such claim, the trustees, the reorganized company and any party in interest may be permitted by the court to object thereto. The reorganized company shall have the right to settle or compromise any such claim with the approval of the court.

SECTION IX

Management

1. The first board of directors of the reorganized company shall consist of five members who shall be appointed by the court

for terms of 1 through 5 years, respectively. The compensation of members of the board of directors for the first year shall be fixed by the court. Any vacancy in the board of directors which occurs prior to the first annual meeting of stockholders of the reorganized company, or which may thereafter occur between annual meetings, shall be filled by majority vote of the members of the board of directors for the balance of the term so vacant. At each of the first four annual meetings of the stockholders of the reorganized company, they shall elect for terms of 1 year that number of directors required to fill the seat or seats of directors whose terms expire at such meeting. Thereafter all directors shall be elected as determined by the stockholders.

2. The first annual meeting of the stockholders of the reorganized company shall be held approximately 1 year, and not later than 15 months, following the confirmation date.

3. The officers of the reorganized company shall be selected, appointed and have their compensation fixed by the board of directors. A director may be an officer of the reorganized company.

SECTION X

Payment of expenses and other allowances

After the confirmation date and prior to the consummation date, expenses of the debtor's estate and allowances to the trustees, their attorneys and experts, and all other expenses of consummation, shall continue to be paid in cash in the manner followed for payment of expenses since the commencement of the reorganization. All final expenses and allowances as may be fixed by the Commission and allowed by the court in accordance with the provisions of section 77(c)(2) and 77(c)(12) of the Bankruptcy Act shall be paid by the reorganized company as provided in the plan.

SECTION XI

Execution of the plan

1. Upon entry by the court of orders permitting the carrying out of the plan, or any part thereof, the debtor shall have the full power and authority to and shall put into effect and thus

carry out the plan and the orders of the court relative thereto, under and subject to the supervision and control of the court, the laws of any State or the decision or order of any State authority to the contrary notwithstanding. In thus carrying out the plan and putting it into effect, the trustees shall act for the debtor and reorganized company until relieved of such functions by the court.

The interests of each class of stockholders and of each class of creditors will not be adversely and materially affected by a transfer of the assets to Penn Central with the consideration therefor made subject to the liens above described, and such transfer, following approval of the court, will not be submitted to any class of stockholders or creditors, other than the United States of America, for acceptance or rejection. Following such transfer of assets, the plan shall be submitted for acceptance or rejection to the creditors of each class whose claims have been filed and allowed and which have been found by the Commission in such orders approving the plan to have an equity, as provided by section 77(e) of the Bankruptcy Act. Thereafter, if the court shall find that the plan has been so accepted, or if the court shall not so find, the trustees shall request the entry by the court of supplemental orders confirming the plan and directing the plan to be consummated.

2. Following entry by the court of supplemental orders confirming provisions of the plan not theretofore confirmed, the trustees shall take all steps as promptly as possible to complete the consummation of the plan and generally to wind up the reorganization proceedings.

3. In carrying out the consummation of the plan, the trustees may employ such agents, transfer agents, registrars, indenture trustees, depositaries, scrip agents, accountants, attorneys and others as they may deem necessary or desirable, subject to the approval of the court.

4. The court will retain jurisdiction over the assets dealt with by the plan, and over any persons appearing in the reorganization proceedings, for the purposes of determining any claims asserted against the debtor or the trustees, construing any order or the plan, and carrying out and giving effect to any and all provisions of the plan and the orders confirming the plan, fixing terms of consummation of the plan, and entering the final decree. Following the transfer of the assets and obligations to Penn Central and payment of the consideration by Penn Central, the court

may cure any defect, supply any omission, or reconcile any inconsistency in such manner or to such extent as may be necessary or expedient in order to carry out the plan effectively.

5. The trustees and the reorganized company shall make all necessary arrangements in connection with the issuance of scrip by the reorganized company in lieu of fractional interests in the new common stock and warrants. Scrip agents shall hold new common stock or warrants underlying the scrip therefor issued under the plan. Holders of scrip will be entitled to receive the new common stock or warrants upon presentation to the scrip agent, holding such new common stock or warrants, of scrip entitled to a full share or a full warrant. A cutoff date shall be provided at which time any new common stock or warrants held by the scrip agents will be sold and the cash proceeds thereof distributed or held for distribution to the holders of the respective outstanding scrip. All expenses of the issuance of scrip, the scrip agents, the sale of securities held by the scrip agents, and the distribution of the proceeds of sale shall be paid by the reorganized company.

SECTION XII

Miscellaneous

1. The property dealt with by the plan, when transferred and conveyed to Penn Central or to the reorganized company, shall be free and clear of all claims of the debtor, its creditors and stockholders and all other persons, unless otherwise specifically provided in the plan or the present report, and the debtor shall be discharged from its debts and liabilities. The court may require the trustees, the debtor, the trustees under any instrument securing an obligation of the debtor, any mortgagee, and all other proper and necessary parties, to make such transfer or conveyances, and may require the debtor to join in any such transfer or conveyance made by the trustees, as may be necessary to consummate the plan.

2. Whenever notice is to be given under the plan, other than by the Commission, the court may designate the time within which, the persons to whom, and the form and manner in which, such notice shall be given. In all notices so designated by the court, unless otherwise specified, such notices shall be given by the trustees.

3. The classification of creditors and stockholders in the plan and all statements contained in the plan as to such classification are conditioned upon the approval and confirmation of the plan. If the plan is not approved or, if approved, is not confirmed, such classification and the proposed treatment shall not be binding upon the debtor or the trustees and shall be without prejudice to the rights of any party in interest and of the trustees; and no statement contained in the plan shall be deemed to be an admission as to the relative rights or interests of any creditor or stockholder.

4. The property to be vested in the reorganized company under the plan shall include all books, files, records, and other papers of the debtor, except such of the same as may be deemed by the trustees or by the court to be necessary in connection with operation of the debtor's transportation properties being sold to Penn Central pursuant to Commission and court orders.

5. The section headings contained in the plan are for convenience only and shall not control or affect the meaning or interpretation of the plan or of any of its provisions.

6. Except as otherwise provided herein, the means of executing the plan and the details of its consummation not otherwise provided for shall be determined by the debtor's board of directors subject to the approval of the court.

COMMISSIONER HARDIN did not participate.

APPENDIX 1

Adjustment of valuation results to December 31, 1966, for depreciation of freight cars in the year 1966

Type of cars	Year built	Number of units December 31, 1966	Liquidation unit price	Estimated remaining life	Estimated scrap value	Unit price less scrap value	Annual depreciation per unit	Total depreciation all units	Penn Central estimate
Freight cars									
Box 40' 55T	1944-1948	2,294	$1,740	6	$450	$1,290	$215	$493,210	$591,852
Box insulated	1953	98	4,000	13	450	3,550	273	26,754	69,380
Box 508 70T Cushion	1965	6	12,000	25	500	11,500	460	2,760	4,596
Hoppers 70T	1953	538	3,000	13	450	2,550	196	105,448	274,380
Gondolas covered 70T	1959	15	8,000	19	450	7,550	397	5,955	11,325
Hoppers covered 70T	1931	30	3,000	5	450	2,550	510	15,300	15,300
Flat (TTX)		2	10,000	15	500	9,500	633	1,266	1,266
Flat 85'	1962	48	10,000	22	500	9,500	432	20,736	45,600
Transformer Heavy duty		22	3,045	5	545	2,500	500	11,000	11,000
Transformer Heavy duty	1954	3	30,000	14	600	28,400	2,100	6,300	8,820
Total								688,729	1,033,719
Difference								344,990	

APPENDIX 2

Equipment type	Gordon sale value at December 31, 1965 (1)	Depreciation, 1966-68						Sale value less 1966-68 depreciation (Column 1- 7)	Balance of obligations at December 31, 1968[3] (9)	Obligations that exceed value (Column 9-8)
		Number of units (2)	Unit sale price (3)	Estimated life at December 31, 1965[1] (4)	Unit price less scrap[2] (5)	Annual depreciation per unit (Column 5 ÷ 4)	3-years of depreciation all units (Column 2 × 6)			
1750 Horsepower diesels	$1,800,000	30	60,000	11	55,000	5,000	450,000	1,350,000	988,571	----------
1800 Horsepower diesels	900,000	15	60,000	11	55,000	5,000	225,000	675,000	450,000	----------
1600 Horsepower diesels	900,000	15	60,000	11	55,000	5,000	225,000	675,000	343,000	----------
1750 Horsepower EA. and diesels	2,250,000	30	75,000	12	70,000	5,833	524,970	1,725,030	2,258,734	2,258,734
1800 Horsepower EL and diesels	2,250,000	30	75,000	15	70,000	4,667	420,030	1,829,700	3,807,720	3,807,720
Hoppers	340,000	85	4,000	14	3,550	254	64,770	275,230		
Sleeping cars	300,000	15	20,000	13	19,000	1,462	65,790	234,210	173,000	----------
Total	----------	----------	----------	----------	----------	----------	----------	----------	----------	$6,066,454

[1]Column 4 represents total useful life less average age at December 31, 1965. For locomotives we use a total useful life of 20 years, and for cars a total useful life of 25 years.

[2]Scrap values of $5,000 per locomotive, $450 per hopper, and $1,000 per sleeping car are assumed consistent with Penn Central's depreciation study for 1968.

[3]Compare exhibits NIII-62, pages 24-26 and NIII-64 with the Report of the Trustees for 1967 to the Reorganization Court, filed March 29, 1968, page 5711 of the printed record, and see exhibit R-3.

APPENDIX 3

Conditions for the protection of EL

Upon inclusion of the NH in the transaction authorized by the Interstate Commerce Commission in Finance Docket No. 21989:

1. Penn Central and EL, as to traffic moving to and from all stations on or reached via the lines of the NH, to or from stations on or reached via the lines of EL, shall with respect to each other maintain and keep open existing or comparable routes and chanhels of trade in full vigor as fast competitive service routes via Maybrook, N. Y., unless and until otherwise authorized by the Interstate Commerce Commission.

2. The present neutrality of handling traffic inbound and outbound by NH shall be continued by Penn Central, insofar as such matters are within its control, so as to permit equal opportunity for service to and from the lines of EL without discrimination as to routing or movement of traffic and without discrimination in the arrangement of schedules or otherwise. Likewise, the present neutrality of handling traffic inbound and outbound by EL shall be continued so as to permit equal opportunity for service to and from the lines of NH included in Penn Central without discrimination as to routing or movement of traffic and without discrimination in the arrangement of schedules or otherwise.

3. The present traffic and operating relationships existing between NH, on the one hand, and EL, on the other, shall be continued, insofar as such matters are within the control of Penn Central, on the one hand, and EL, on the other.

4. Insofar as such matters are within its control, Penn Central shall, as to the lines of NH included in the transaction authorized in Finance Docket No. 21989, accept, handle, and deliver all cars inbound and outbound, loaded and empty, without discrimination in service as between cars destined to or received from EL, and carriers competing with EL, and irrespective of destination or route of movement. Likewise, EL shall accept, handle, and deliver all cars inbound and outbound, loaded and empty, without discrimination in service as between cars destined to or received from the lines of NH included in the transaction authorized in Finance Docket No. 21989 and carriers competing with said lines of Penn Central, and irrespective of destination or route of movement.

5. Penn Central shall not do anything to restrain or curtail the right of industries now located on the lines of NH to route traffic over existing or comparable routes via Maybrook in connection with EL. Likewise, EL shall not do anything to restrain or curtail the right of industries now located on its lines to route traffic over existing or comparable routes via Maybrook in connection with the lines of the NH included in the transaction authorized in Finance Docket No. 21989.

6. Insofar as such matters are within their control, Penn Central, on the one hand, and EL, on the other, shall cooperate with each other and each shall use its best efforts with its connections to obtain similar cooperation in order to continue the NH-EL route as a competitive service route for the

movement of freight traffic between points located on or beyond NH's lines and points located on or beyond EL's lines, endeavoring at all times to improve such service and maintaining at least the same standards of service as prevail on the date of the inclusion of NH in Penn Central. Neither EL, on the one hand, nor Penn Central, on the other, shall without the written consent of the other, make any substantial change in train schedules or take any other action, the effect of which would be to increase the time in transit via the aforesaid routes, or to otherwise adversely affect the standards of service.

7. With respect to traffic presently handled jointly by the NH, on the one hand, and EL, on the other, Penn Central and EL will, insofar as such matters are within their control, continue to publish or concur in publication of rates so that rates to or from points on or reached via EL routes will always be competitive with other routes, including the local routes of Penn Central, and as to the aforesaid traffic they shall also concur in divisions of such rates under the established bases of divisions, and in the event of any changes in joint rates proportionate changes shall be made in the divisions of Penn Central and EL.

8. Any party or person having an interest in the subject matter may at any further time make application to the Commission for such modification of the above conditions, or any of them, as may be required in the public interest, and jurisdiction shall be retained by the Commission to reopen the proceeding on its own motion for the same purpose.

9. These conditions shall become effective as of the date of inclusion of NH in Penn Central and upon their acceptance by EL, evidenced in writing to the Commission.

10. Penn Central and EL will distribute copies of this appendix, and any amendments which may from time to time be made or accurate summaries thereof, to all of their operating officers, traffic officers, and traffic representatives, in order that all operating and traffic personnel of EL, and Penn Central will be at all times advised of the purposes and effects of this appendix.

11. The interpretation, application and enforcement of the conditions of this appendix shall be governed exclusively by the following provisions:

A. All controversies arising under this appendix (except those relating to the modification of conditions referred to in condition 8) shall be determined with finality by the Interstate Commerce Commission in the manner indicated below. Orders of this Commission, made as provided hereinafter, shall not be reviewable in any court. Orders of this Commission determining any such controversy may be enforced by judicial order or judgment as provided in 49 U.S.C. § 16.

B.(1) Whenever EL or Penn Central considers that these protective conditions are being violated, it may file with the Commission, Board of Suspension, and with the other carrier, a complaint verified by an appropriate official of the complainant, containing a short and plain statement of the matters constituting the alleged violation and the relief sought.

(2) If, in the case of a complaint involving a tariff publication, such complaint shall include a prima facie showing that EL is a competitive

factor as to traffic affected by such tariff, the Board of Suspension may, in the case of a tariff publication already effective, and shall in the case of a tariff publication not yet effective, forthwith suspend such tariff pending determination by the Board of the issues presented by such complaint. Said Board shall conduct an investigation of the matters referred to in any complaint and, if requested by any party to the controversy, shall hold a hearing. If, after such investigation and hearing, if any, said Board shall find no violation of any of the conditions of this appendix, it shall thereupon order the removal of any tariff suspension theretofore imposed. If, after such investigation and hearing, if any, said Board shall find a violation of any of the conditions of this appendix, it shall thereupon order the cancellation of any violative tariff provisions or, if no tariff be involved, the termination of any violative conduct.

C. (1) Final decisions as to issues raised by a complaint shall be rendered by the Board of Suspension within 90 days after the complaint is filed.

(2) Appeal shall lie to the Commission, Division 2, from orders of the Board of Suspension.

(3) Special rules for proceeding before the Board of Suspension and appealing therefrom shall be promulgated by this Commission at a future time. Such rules shall include provisions which afford to Penn Central and to EL full and adequate opportunity to reply to any complaint filed under subdivision B and to present evidence, briefs and argument as to all issues.

APPENDIX 4

Classification of claims and securities to be issued under provisions of NH reorganization plan.

Class	Classification of claim	Amount of claim December 31, 1968	Satisfaction of claims	
			Amount	Description
	Administration claims			
A	Costs and expenses of reorganization	$5,000,000	$5,000,000	Installment notes and cash
B	Trustees' certificates	12,500,000	12,500,000	Certificates extended
C	Flood and shop loans	1,747,000	1,747,000	Paid currently
D	Postbankruptcy taxes	19,697,000 Est.	19,697,000	Income notes
E	Postbankruptcy per diem	15,850,000 Est.	15,850,000	Income notes
F	Other administration claims	10,821,000	10,821,000	Income notes
	Total	65,615,000	65,615,000	
	Prebankruptcy claims			
G	Claims of United States	15,335,000		No payment
H	State and local taxes	6,707,000	6,707,000	Income notes
I	Harlem River bonds:			
	Principal	6,647,000		Assumed by Penn Central
	Interest	2,260,000		Assumed by Penn Central
J	First mortgage bonds:			
	Principal	76,820,000	1,536,398 shares	Common stock, $50 principal
	Interest	24,840,000	993,600 warrants	Warrants, $25 accrued interest
K	Income bonds-principal	52,756,000	1,055,110 warrants	Warrants, $50 principal
L	Equipment obligations	13,181,000		Assumed by Penn Central
M	Other claims found secured	(unknown)		Income notes
N	Unsecured claims	21,767,000		No provision
O	Interest of stockholders	48,400,000		No provision
	Total	268,713,000		

APPENDIX 4—Continued

Capital structure of reorganized company

Kind of security	Period	Interest	December 31, 1968	December 31, 1970
Installment notes	5 annual installments	None	$5,000,000	$5,000,000
Income notes	7 years	5 percent contingent cumulative.	53,000,000	55,150,000
Trustees, certificates	7 years	5½ percent-sinking fund-	12,500,000	12,500,000
Total			[1]70,500,000	72,650,000
Common stock-shares			1,536,398	1,536,398
Warrants-number of			2,048,710	2,284,228

[1]The income notes shown in the first portion of this appendix aggregate $53,075,000. This amount rounded out to $53 million, plus the other securities, equal $70,500,000.

APPENDIX 5

I. Net cash required[1] to support capital structure if trustees' plan of reorganization is consummated December 31, 1970

Line No.	Debt securities (1)	Principal amount (2)	First year (3)	Second year (4)	Third year (5)	Fourth year (6)	Fifth year (7)	Sixth year (8)
1.	Trustees' certificates	$12,500,000	$656,000	$656,000	$656,000	$1,906,000	$1,841,000	$1,775,000
2.	Installment notes	5,000,000	----------	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000
3.	Income notes	55,150,000	2,758,000	2,758,000	2,758,000	2,758,000	2,758,000	2,758,000
	Total	72,650,000	3,414,000	4,414,000	4,414,000	5,664,000	5,599,000	5,533,000

[1]Net of cash requirements for corporate expenses.

APPENDIX 5—Continued

II. *Sources of net cash*[1]

Debt securities (1)	Principal amount (2)	First year (3)	Second year (4)	Third year (5)	Fourth year (6)	Fifth year (7)	Sixth year (8)
Anticipated interest and proceeds from Penn Central bonds	$33,600,000	$1,680,000	$1,680,000	$1,680,000	$2,597,000	$2,551,000	$2,506,000
Total dividends required on Penn Central stock	950,000 (shares).	1,734,000	2,734,000	2,734,000	3,067,000	3,048,000	3,027,000
Total		3,414,000	4,414,000	4,414,000	5,664,000	5,599,000	5,533,000

[1]Net of cash requirements for corporate expenses.

APPENDIX 6

Effect of consummation of trustees' plan of reorganization

I. *Initial assets excluding current assets*

Penn Central-bonds	[1]$33,600,000
Penn Central-stock	950,000 shares

II. *Stockholders' equity based on various valuations for Penn Central stock*

Penn Central stock market price	$87.5	$100	$125	$150	$175	$200
Total asset value[2]	116,725,000	128,600,000	152,350,000	176,100,000	199,850,000	223,600,000
Debt securities	72,650,000	72,650,000	72,650,000	72,650,000	72,650,000	72,650,000
Shareholders' equity	44,075,000	55,950,000	79,700,000	103,450,000	127,200,000	150,950,000
Net asset value per share	29	36	52	67	83	98
Indicated value of warrants[3]	----------	----------	2	17	33	48

III. *Equivalent stock and warrant value*

1. Per $1,000 first mortgage bonds	580	720	1,072	1,612	2,188	2,728
2. Per $1,000 income bonds	----------	----------	40	340	660	960

[1]Includes $31.5 million of bonds relating to purchase price, and $2.1 million relating to purchase price adjustments.

[2]Consisting of $83,125,000 of Penn Central stock and $33,600,000 of Penn Central bonds. This does not include any balance of the $2.7 million of cash described in appendix 7.

[3]Excess of net asset value over exercise price of $50 per share assuming no exercise of warrants.

APPENDIX 7

Pro-forma statement of cash deposits and deductions of the debtor giving effect to the consummation of the inclusion[1]

Cash Deposits:		
Court fund, U. S. District Court		$ 7,204,682
Sale of mortgaged property		623,385
		7,828,067
Temporary cash investments		2,325,683
Special deposit retained		194,943
Interest and dividends receivable		8,164
		10,356,857
Cash on hand June 30, 1968		1,317,691
Cash payment—Penn Central		8,000,000
Total		19,674,548
Deductions:		
Section 7 adjustments		8,246,714
Employees' vacations—in escrow		5,798,154
		14,044,868
		5,629,680
Cash payments of current obligations:		
Interest payments	$ 98,750	
Attorneys' fees, et cetera	414,514	
Leased lines taxes	545,591	
Other taxes	145,951	
Flood and shop loans	1,747,000	
Total		2,951,806
Remainder for cash payment of current obligations		2,677,874

[1] Each of the figures is as of June 30, 1968, except the cash payment from Penn Central, the section 7 adjustments, and the flood and shop loans.

ORDER

At a General Session of the INTERSTATE COMMERCE COMMISSION, held at its office in Washington, D. C., on the 25th day of November 1968.

Finance Docket No. 21989

PENNSYLVANIA RAILROAD COMPANY—MERGER—NEW YORK CENTRAL RAILROAD COMPANY

Finance Docket No. 21990

PENNSYLVANIA RAILROAD COMPANY STOCK ISSUANCE

Finance Docket No. 24361

PENNSYLVANIA RAILROAD COMPANY SECURITIES AND ASSUMPTION OF OBLIGATIONS

Finance Docket No. 21669

NEW YORK, NEW HAVEN & HARTFORD RAILROAD COMPANY REORGANIZATION

Finance Docket No. 24756

NEW YORK, NEW HAVEN & HARTFORD RAILROAD COMPANY TRUSTEES' CERTIFICATES

Investigation of the matters and things involved in these proceedings having been made, a further hearing having been held and the Commission, on the date hereof, having made and filed its fourth supplemental report containing its findings of fact and conclusions thereon, which report is hereby referred to and made a part hereof:

It is ordered, That the reports and orders of November 16, 1967, and March 1, 1968, be, and they are hereby, modified in accordance with the findings of said fourth supplemental report, and as so modified, reinstated and affirmed;

It is further ordered, That, as of January 1, 1969, which is the day following the closing date under the purchase agreement referred to in the aforesaid reports, the Penn Central Company be, and it is hereby, required to include within its system The New York, New Haven and Hartford Railroad Company under such terms and conditions in the second and third supplemental reports and orders as modified and affirmed in the fourth supplemental report and order herein, as pertain to the payment of consideration and assumption of obligations by the Penn Central Company, and the conveyance to it of the properties and franchies of The New York, New Haven and Hartford Railroad Company, subject to such action by the reorganization court as is necessary to effect the said conveyance; that the Penn Central Company take such steps as are necessary to effect the inclusion on the date ordered herein, and that such inclusion be effected regardless of then pending petitions for reconsideration or matters in litigation, unless prior thereto, the effectiveness of this order has been enjoined by lawful court order;

It is further ordered, That, subject to the approval of the reorganization court, the trustees of The New York, New Haven and Hartford Railroad Company, be, and they are authorized to convey the properties and franchises of said railroad to the Penn Central Company and to receive payment of consideration (including the transfer of obligations) from the Penn Central Company under the terms and conditions referred to in the immediately preceding paragraph of this order;

It is further ordered, That subject to the conditions for protection of railway employees and other terms and conditions referred to in said fourth supplemental report, the inclusion in the Penn Central Company of the Providence and Worcester Railroad Company and the Norwich and Worcester Railroad Company be, and it is hereby, approved and directed;

It is further ordered, That the plan of reorganization of The New York, New Haven and Hartford Railroad Company, debtor, set forth in said fourth supplemental report, and incorporated herein, be, and it is hereby, approved;

It is further ordered, That the conclusions and findings in said fourth supplemental report are not to be construed as a

grant of authority for the issuance or assumption of obligations, by the reorganized New Haven Railroad Company;

It is further ordered, That the order of November 16, 1967, in Finance Docket No. 24361, be, and it is hereby, modified to authorize issuance by the Penn Central Company (formerly known as The Pennsylvania Railroad Company) to the trustees of The New York, New Haven and Hartford Railroad Company of $33,600,000 principal amount of 25-year Divisional First Mortgage bonds or such principal amount of bonds as may result from operation of the purchase price adjustment provisions, in lieu of the $23 million principal amount previously authorized; and except as so modified, the security issue and assumption of obligation provisions of said order of November 16, 1967, are confirmed and continued;

It is further ordered, That the journal entries covering the necessary accounting required in affecting the authorities herein granted and executing the plan herein approved shall be submitted to this Commission for approval; and

It is further ordered, That the jurisdiction of this Commission be, and it is hereby, retained in these proceedings, for the purpose of making such further order or orders as may be necessary or appropriate, in addition to those orders under jurisdiction expressly retained in the prior reports and orders of the Commission and to those orders which may be issued under section 5(9) of the Interstate Commerce Act.

By the Commission.

H. NEIL GARSON,

(SEAL) Secretary.

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FINANCE DOCKET NO. 21989[1]

PENNSYLVANIA RAILROAD COMPANY–MERGER–NEW YORK CENTRAL RAILROAD COMPANY

Decided July 10, 1969
As modified August 26, 1969

On further consideration, prior reports and orders of November 16, 1967, March 1, 1968, and November 25, 1968, affirmed as modified with respect to property valuation and other matters. Prior reports 327 I.C.C. 475, 328 I.C.C. 304, 330 I.C.C. 328, 331 I.C.C. 643, 331 I.C.C. 754, and 334 I.C.C. 25.

Appearances as shown in prior reports.

FIFTH SUPPLEMENTAL REPORT OF THE COMMISSION ON RECONSIDERATION

BY THE COMMISSION:

On June 18, 1969, the United States District Court for the Southern District of New York entered an opinion largely sustaining our *fourth supplemental* report of November 25, 1968, 334 I.C.C. 25. This opinion followed by less than 1 month the Memorandum of Decision by the United States District Court for the District of Connecticut, sitting as a reorganization court, in its docket No. 30226, holding important features of the valuation and pricing set forth in the *fourth supplemental* report to be unlawful.

The opinion of the three-judge court includes several other holdings reversing our valuation and pricing findings in lesser important areas involving relatively insubstantial sums. The opinion directs us, (1) to prepare and serve a proposed decree which, "among other things, shall reflect in dollar amounts the changes directed in this opinion," and (2) that our order accompanying the *fourth supplemental* report be modified as provided in the opinion of the reorganization court on the issue of the value of the Penn Central stock delivered to the estate.

We conclude that no appeal should be taken by this Commission from the decision of the three-judge court, and that an appeal

[1] Embraced herein are Finance Docket No. 21990, Pennsylvania Railroad Company Stock Issuance; and Finance Docket No. 24361, Pennsylvania Railroad Company Securities and Assumption of Obligations.

should be taken by the Commission from the decision of the reorganization court only insofar as it differs from the decision of the three-judge court. Although we have decided not to appeal, we cannot escape the necessity for making our own new findings as to whether the higher consideration to be paid by Penn Central for the New Haven properties, consistent with the three-judge court's conclusions on several issues of valuation and price, constitutes "equitable terms" within the meaning of section 5(2)(d) of the Interstate Commerce Act. Moreover, to the extent that, consistent with that court's decision, Penn Central is required to issue to the New Haven estate securities in excess of those which we have authorized previously pursuant to section 20a of the Interstate Commerce Act, our further authorization and requisite findings are required to validate such additional securities.

We conclude as a matter of independent judgment, that we now can and should upon the present record arrive at supplemental findings and conclusions, consistent with the decision of the three-judge court, which will facilitate final disposition of this prolonged proceeding. We trust that the following computations and other findings will be helpful to the court, whether it desires to embody the concurrent findings and conclusions in a detailed decree, or simply to sustain our decision as now supplemented. These proceedings are reopened for reconsideration on our own motion on the record as made for the limited purposes described in the following paragraphs, the subject matter of which has been discussed in our prior reports.

Grand Central Terminal Properties.–For reasons stated in the opinion of the three-judge court, we find that the amount of $3.38 million, which includes an adjustment of hotel earnings (amounting to $655,000), should be paid by Penn Central as New Haven's one-half share of the excess income in 1967 and 1968 from the Grand Central Terminal properties;

Accrued real estate taxes and New Haven's investment in B&P.–For reasons stated in the opinion of the three-judge court, we find that Penn Central should be refunded $1.5 million, which was the value we attached to New Haven's share of the Boston & Providence CCBI's; and that Penn Central should pay $1.6 million, which was a discount we attached to New Haven's future liability for accrued real estate taxes;

Discount to present worth.–We find that consistent with our Chairman's letter of June 10, 1969, to the reorganization court,

exclusive of the item relating to the Harlem River and Oak Point Yards, and consistent with the opinion of the three-judge court, the discount to present worth should be reduced by $410,000, and hence Penn Central should be required to pay such additional sum, computed as follows:

Adjustment of discount to present value

Items affecting liquidation proceeds	First year	Second year	Third year	Total change
		In millions		
(a) New Haven's interest in B&P	+$1.1			+$1.1
(b) Value of property:				
Equipment	-3.5			-3.5
Road property	-0.9	-$0.9	-$0.9	-2.7
	-4.4	-0.9	-0.9	-6.2
(c) Depreciation for 1966:				
Equipment	-2.3			-2.3
Road property	-0.3	-0.2	-0.2	-0.7
	-2.6	-0.2	-0.2	-3.0
Net change in proceeds	-$5.9	-$1.1	-$1.1	-$8.1
Discount at annual rate of 6 percent:				
Discount factors	0.02913	0.08486	0.13739	
Amount of discount	-$0.17	-$0.09	-$0.15	-$0.41

Harlem River Division bonds.—We find that consistent with the opinion of the three-judge court, an appropriate discount of the Harlem River Division bonds assumed by Penn Central on December 31, 1968, is $483,270, computed as follows:

When payable	Percent	Amount payable	Discount factor	Amount of discount
Accrued interest:				
On date of inclusion, 1968	20	$452,000		
First year, 1969	20	471,210	.056604	$26,672
Second year, 1970	20	490,420	.110004	53,948
Third year, 1971	20	509,630	.160381	81,735
Fourth year, 1972	20	528,840	.207906	109,949
Subtotal	100	2,452,100		272,304
Credit for interest on accrued interest		192,100		
Future interest:				
First year, 1969		282,498	.056604	15,991
Second year, 1970		282,498	.110004	31,076
Third year, 1971		282,498	.160381	45,307
Fourth year, 1972		282,498	.207906	58,733
Subtotal		1,129,992		151,107
Credit for payment of interest		1,129,992		
Principal:				
January 1, 1973		6,647,000	.207906	1,381,951
Total (less *credits*)				483,270

Additional consideration to be paid New Haven.–We find that it is just, reasonable, equitable, and consistent with the public interest that Penn Central shall pay the New Haven additional consideration, exclusive of the settlement required by section 7 of the purchase agreement which shall include a cash settlement of accrued excess income for 1967 and 1968, totalling $99,000 computed as follows:

	In millions
B&P CCBI's	– $1.50
Accrued real estate taxes	+ 1.60
Reduction in discount to present worth	+ 0.41
Assumption of Harlem River Division bonds	+ 0.48
Additional consideration excluding accrued excess income	+ 0.99

We further find that a "mix" of additional consideration of $990,000, composed of cash, stock, and bonds in the relative amounts set forth in the *fourth supplemental* report, is just and reasonable and upon entry of a final order by the three-judge court, and by the Supreme Court sustaining such order if an appeal is timely filed, the Penn Central Company shall pay, consistent with the court's opinion, the additional consideration of $990,000 in the following "mix."

	Percent	Amount
Stock	57.1	$565,290
Bonds	37.4	370,260
Cash	5.5	54,450
Totals	100.0	990,000

In addition to cash, and in order to comply with the foregoing paragraph, Penn Central shall issue to the trustees of The New York, New Haven and Hartford Railroad Company, (a) 6,460 shares of its common stock of the par value of $10 per share, and additional shares that may be made necessary by the anti-dilution provisions referred to in the *inclusion* report, and (b) $425,799 principal amount of 25-year divisional first mortgage bonds (or 23/20 of $370,260).

We find that the issuance by the Penn Central Company of its common stock and 25-year divisional first mortgage bonds is for lawful objects within the corporate purposes of Penn Central

Company and compatible with the public interest, necessary and appropriate for and consistent with the proper performance by it of service to the public as a common carrier, will not impair its ability to perform that service, and is reasonably necessary and appropriate for such purposes.

The findings set forth in the foregoing paragraph equally apply in a broad sense to the suggestion of the reorganization court that Penn Central should underwrite to February 1, 1978, the 950,116 shares, and any additional shares, Penn Central has been or will be required to transfer to the New Haven; however, such findings, as well as appropriate findings under section 5, cannot be made until many details of an underwriting formula are resolved, such as (1) what specific price should govern during the 5-day period referred to by the reorganization court, (2) what is the effect of a recapitalization of Penn Central or stock split or stock dividend, (3) what is Penn Central's liability in 1978 if the estate has sold a portion of its holdings above $87.50 per share, or above the 30-day mean price, and (4) what provision should be made for unforeseen contingencies or what jurisdiction should be reserved in order to ensure that Penn Central's obligation shall not exceed but shall not be less than $87.50 per share. Accordingly, upon entry of a final order by the three-judge court and by the Supreme Court sustaining such order, if an appeal is timely filed, we will entertain written representations from any party regarding the precise terms of an underwriting requirement in order to enable us to incorporate such a requirement in our decision.

We conclude and find, that as modified and supplemented herein our prior reports in 331 I.C.C. 643, 331 I.C.C. 754, and 334 I.C.C. 25 are affirmed and continued.

An appropriate order will be entered.

COMMISSIONER HARDIN did not participate.

334 I.C.C.

ORDER

At a General Session of the INTERSTATE COMMERCE COMMISSION, held at its office in Washington, D.C., on the 26th day of August 1969.

Finance Docket No. 21989

PENNSYLVANIA RAILROAD COMPANY—MERGER—NEW YORK CENTRAL RAILROAD COMPANY

Finance Docket No. 21990

PENNSYLVANIA RAILROAD COMPANY STOCK ISSUANCE

Finance Docket No. 24361

PENNSYLVANIA RAILROAD COMPANY SECURITIES AND ASSUMPTION OF OBLIGATIONS

Reconsideration of the matters and things involved in these proceedings having been made and the Commission, on the date hereof, having made and filed its fifth supplemental report containing its findings of fact and conclusions thereon, which report is hereby referred to and made a part hereof:

It is ordered, That the reports and orders of November 16, 1967, March 1, 1968, and November 25, 1968, be, and they are hereby, modified and supplemented in accordance with the findings of said fifth supplemental report, and except as so modified and supplemented, continued in full force and effect;

It is further ordered, That the orders of November 16, 1967, and November 25, 1968, in Finance Docket No. 24361, be, and they are hereby, modified, to authorize issuance by the Penn Central Company to the trustees of The New York, New Haven and Hartford Railroad Company of an additional 6,460 shares of its common stock of the par value of $10 per share and additional shares that may be made necessary by the antidilution provisions referred to in the inclusion report in these proceedings, 331 I.C.C. 643, and of an additional $425,799 principal amount of 25-year divisional first mortgage bonds, for the pur-

poses set out in said fifth supplemental report; and, except as so modified, the security issue and assumption of obligation provisions of said orders of November 16, 1967, and November 28, 1968, are confirmed and continued;

And it is further ordered, That the jurisdiction of this Commission be, and it is hereby, retained in these proceedings, for the purpose of making such further order or orders as may be necessary or appropriate, in addition to those orders under jurisdiction expressly retained in the prior reports and orders of the Commission and to those orders which may be issued under section 5(9) of the Interstate Commerce Act.

By the Commission.

ANDREW ANTHONY, JR.,

(SEAL)

Acting Secretary.

IN THE

UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF CONNECTICUT

In Proceedings for the Reorganization of a Railroad

In the Matter of
THE NEW YORK, NEW HAVEN AND HARTFORD RAILROAD COMPANY,
Debtor.

No. 30226

MEMORANDUM OF DECISION ON PETITION FOR ORDER #441; CROSS-PETITIONS OF FIRST MORTGAGE BONDHOLDERS COMMITTEE AND OF OSCAR GRUSS & SON FOR TERMINATION OF REORGANIZATION PROCEEDINGS, AND TRUSTEES' MOTIONS TO DISMISS THE CROSS-PETITIONS.

On April 5, 1967 the Trustees for the Debtor in reorganization filed a petition requesting instructions from the court as to their future course of action. At that time the prospect for the continued operation of the Railroad was very dim. From the time when they were appointed in July of 1961, the Trustees had been of the opinion that the best means for assuring the survival of the New Haven lay in the direction of merger with a large trunkline railroad. They were the first to evince an understanding of this now obvious truth, and they were the first to propose intervention in the proceedings, instituted March 9, 1962, before the Interstate Commerce Commission for the merger of the Pennsylvania and New York Central Railroads, which culminated in the Commis-

sion's order that the New Haven must be included in that merger. At the time of their appointment the New Haven was losing cash at a rate of approximately $1,500,000 per month. This lethal attrition was in a few months not only arrested but the cash position was significantly improved over the ensuing years. Meanwhile, however, in spite of spartan economies and a sizeable reduction in numbers of employees, the costs of operation, chargeable principally to various forms of competition and to repeated increases in payroll expenditures, brought about by settlements between the National Railway Labor Conference and the National Unions, off-set savings and eroded away the accumulated cash. Cash assistance was sought from the Federal Government and the four States involved. The former furnished a guaranty for loans up to $12,500,000 but there were no grants of cash except that Connecticut continued its grant of $500,000 per year for maintenance of underpasses and bridges. Considering that the operation of the Railroad was of sufficient size to involve a payroll of $1,500,000 per *week*, it can be said that no substantial cash aid was forthcoming until mid 1965 when the four States agreed on contributions totalling approximately $5,500,000 per year which was only one-third to one-fourth of the New Haven's net operating losses.

The merger petition of the Pennsylvania and New York Central Railroads was approved by the Interstate Commerce Commission and an application to enjoin the immediate consummation of the merger was refused by a three-judge federal district court in the Southern District of New York, but on March 27, 1967 the Supreme Court reversed the judgment of the District Court and remanded the case to the Interstate Commerce Commission for further proceedings. *Baltimore & Ohio Railroad Co.* v. *United States*, 386 U.S. 372 (1967).

In Petition for Order #441 the Trustees of the New Haven recounted the continuing financial deterioration of the Railroad and estimated sizeable cash losses for 1967. They also mentioned the serious likelihood of protracted delay in the culmination of the Penn-Central merger and the inability of the New Haven to continue its operations short of tapping funds in the registry of the

court. It was in the light of these circumstances that instruction from the court was sought. The cross-petitioners, First Mortgage 4% Bondholders Committee and Oscar Gruss & Son, asked either for an immediate take-over of the New Haven by the Penn-Central, once the merger was approved, or for the termination of the reorganization proceedings and liquidation of the Railroad. A partial hearing on petition for Order #441 was held.

Soon after the filing of the cross-petitions, however, it became apparent that an extraordinary effort was being made by the Interstate Commerce Commission and the parties in interest in the Penn-Central merger to accelerate the rehearing and disposition of the case on remand. The Commission issued its decision on the merger and allied matters on June 9, 1967 and, in expedited proceedings, the appeals were heard by a three-judge court in the Southern District of New York which rendered its decision on October 19, 1967 dismissing all of the complaints attacking the merger and inclusion orders and affirming the decisions of the I.C.C.

In view of these developments and the assurance from those representing the four States that every effort would be made to continue their cash assistance at approximately the same rates, the court postponed the completion of hearings on the petition for Order #441 and the cross-petitions, and in so doing denied several requests by the cross-petitioners to hold the hearings and terminate the reorganization proceedings.

In July, 1967, it had appeared likely that the cash would be so depleted that operation of the Railroad would have to be terminated by the end of September if by that time there was no improvement. At that time the court was not only concerned by the possibility that such a cessation of operations might be brought about by the loss of cash before the effective date of the Penn-Central merger, assuming that a favorable decision were handed down by the Supreme Court, but also by the lack of cash resources between the time of the merger and the date on which the operation of the New Haven would be taken over by the Penn-Central. Therefore, on July 11th the court issued a partial

ruling on the petition for instructions, calling for an application to the I.C.C. requesting the Commission to fashion, and implement with appropriate orders, a means which would insure the continuation of operations during the period following the merger. Ultimately this was provided by the order of the I.C.C. of November 16, 1967.

Actually by September, 1967, there was some increase in cash from various sources; and, by carefully husbanding its resources, the Trustees were able to keep the Railroad going through the balance of the year while the appeals from the judgments of the three-judge court in the merger and inclusion cases were taken to and heard by the Supreme Court. On January 15, 1968 that Court affirmed the judgments of the three-judge court.

The cross-petitioners have continued to urge that the reorganization proceedings be terminated and that the Railroad be liquidated. It is their position that a continuation of the operations of the Railroad at a loss constitutes a taking of their property without due process and without just compensation. The Trustees have moved to dismiss the cross-petitions for failure to state claims upon which relief can be granted.

From the time of the I.C.C.'s order of April 8, 1966, making inclusion of the New Haven a condition of the Penn-Central merger, to the present, every opinion of every court has accepted or expressly approved the inclusion of the New Haven in the merged Penn-Central system. The Supreme Court in its decision of January 15th, approving the Penn-Central merger and dealing with the present cross-petitioners' argument that inclusion of the New Haven should be required to take place coincidentally with the merger itself "because continued operation of the New Haven at a loss involves progressive erosion of the bondholders' security . . .", laid great emphasis on the importance of the public interest in the continued operation of the New Haven and quoted with approval the I.C.C.'s statement that, "It is a fundamental aspect of our free enterprise economy that private persons assume the risks attached to their investments, and the NH creditors can expect no less because the NH's properties are devoted to a

public use." *Penn-Central and N & W Inclusion Cases*, 36 U.S.L. Week 4093, 4099 (U. S. Jan. 15, 1968). It nowhere even remotely suggested that the interest of the bondholders could not or would not be protected by the regular proceedings before the I.C.C. and subject to review by this court or by a three-judge district court. Justice Fortas' opinion for the majority said:

> "While the rights of the bondholders are entitled to respect, they do not command Procrustean measures. They certainly do not dictate that rail operations vital to the Nation be jettisoned despite the availability of a feasible alternative. The public interest is not merely a pawn to be sacrificed for the strategic purposes or protection of a class of security holders whose interests may or may not be served by the destructive more."
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> *Penn-Central and N & W Inclusion Cases, supra*, at 4099.

The Commission has approved the first or vital portion of a two-step plan of reorganization, which is about to be certified to this court for review. The Commission has found that the plan of reorganization is feasible and that it is fair and equitable in its terms. The Supreme Court opinion made it abundantly clear that it approved the Commission's conclusion that the continuation of the operations of the New Haven was essential and this could be effectuated only by prompt consummation of the Penn-Central merger. It follows that the inclusion of the New Haven must be accomplished as soon as possible and that meanwhile the Trustees are expected to continue operating the New Haven. These are the objectives now to be pursued.

The cross-petitioners argue that the Supreme Court decision did no more than decide at the time that "the Penn-Central merger should not be enjoined." But it should hardly be necessary to point out that the Court's opinion devoted a great deal of discussion to the circumstances of the New Haven Railroad and the affect of the merger upon it. The claims of the bondholders and their fears for the diminishing value of the New Haven's

assets through continued deficit operations was expressly noted and considered. It said, "The bondholders' objections may be registered and adjudicated in the reorganization court or upon judicial review as provided by law." The cross-petitioners argue that the Supreme Court in using these words, has in effect, given its blessing to their present effort to have the reorganization proceedings terminated and to bring about the liquidation of the Railroad. But the Supreme Court opinion cannot be so interpreted. Its mention of the reorganization court and a reviewing court, i.e. a statutory three-judge court, as tribunals in which the bondholders' objections might be registered clearly refers to the present appeal from the I.C.C.'s order of November 16, 1967 and the certification of the approved plan to the reorganization court. It did not contemplate or consider a collateral attack such as that contained in the cross-petitions. The cross-petitioners argue that their petitions were filed in April, 1967, long before the I.C.C.'s order, and it should therefore have precedence. But the I.C.C.'s order was only a culminating step in the long and difficult struggle carried on by the Trustees of the New Haven and their counsel, beginning in June of 1962, for the inclusion of the Debtor in the Penn-Central merger. To jettison everything achieved and turn back just as a glimmer of light begins to show at the end of a long dark tunnel not only carries with it an aura of unreality but borders on the fantastic.

In any event, the cross-petitioners will have ample opportunity to present their claims of lack of due process and a taking of their property without just compensation before the reviewing courts, because, if the evidence in the record of the case before the I.C.C. shows without contradiction that the Commission's order is in violation of the bondholders' constitutional rights, it cannot stand, and the approved plan certainly cannot be found to be fair and equitable.

The real crux of the dispute here concerns the amount that the Penn-Central should be required to pay for the assets of the New Haven. This in turn depends largely on valuation. The cross-petitioners assert that the highest amount will only be realized

through liquidation. They say that the I.C.C. fixed what they call the "net" liquidation value as of December 31, 1966 and that depletion since that date through operational losses has prejudiced their constitutional rights. But the I.C.C. obviously did not interpret its own report and order as conceding that its liquidation figure was as "net" as the cross-petitioners claim they made it. The Commission in its November 16, 1967 report said:

> "If the creditors believe that it is to their advantage to have the reorganization proceeding dismissed and the NH liquidated in an equity proceeding, it is manifest that, unless the States were induced to maintain and, in fact, increase their aid, the creditors might well have to carry the NH's operating losses until those proceedings were completed and the NH were allowed to abandon its operations, even assuming the NH's creditors' position were sustained by the reorganization court and this Commission. It is clear to us from the record that the NH's creditors would not gain from such a procedure."

The cross-petitioners are apparently the only ones who seek liquidation. Neither the trustees for any of the series of bonds nor any other creditors have joined in the cross-petitions.

It would be an abuse of discretion and error on the part of this court to entertain and approve of action by the cross-petitioners designed to scuttle the entire reorganization proceeding when such a course, which the I.C.C. has declared would, at best, be of no benefit to the creditors, was not indorsed by other representatives of the bondholders or creditors and at a time when the prescribed steps under §77 of the Bankruptcy Act have reached their final stages and a plan of reorganization under the Act has been found to be feasible, and a specific plan has been approved and is about to be certified to this court. The cross-petitioners have no right to maintain what in essence is a collateral attack on the Commission's order and report which are subject to statutory provisions for direct review, toward which steps have already been taken. Moreover, the necessity for taking action on petition for Order #441, for instructions by the court to the Trustees for the Rail-

road, has passed. It is, therefore, ordered that the petition for Order #441 and the cross-petitions are dismissed.

Dated at New Haven, Connecticut, this 13th day of February, A.D. 1968.

ROBERT P. ANDERSON
United States Circuit Judge, sitting by designation as United States District Judge.

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF CONNECTICUT

In Proceedings for the Reorganization of a Railroad

In the Matter of THE NEW YORK, NEW HAVEN AND HARTFORD RAILROAD COMPANY, Debtor.	No. 30226

MEMORANDUM OF DECISION ON REORGANIZATION PLAN

On March 29, 1968, pursuant to §§77(d and e) of the Bankruptcy Act, the Interstate Commerce Commission certified to this court the first step of a plan of reorganization of the Debtor, the New Haven Railroad, which it had approved by its order of November 16, 1967.[1] Shortly thereafter the court gave due notice to all parties in interest of the time within which objections to the plan might be filed and of the date, subsequent thereto, when the parties would be heard for or against "such objections to the plan," and on any claims for equitable treatment. On April 8, 1968 this court appointed the Honorable John Van Voorhis as Special Master, under the authority of §77(c)(13) of the Bankruptcy Act, to hear and report respecting the New Haven's right, title or interest in the Grand Central Terminal properties. Thereafter Judge Van Voorhis held hearings, took evidence and filed a report on June 18, 1968, and a supplemental report on June 24, 1968. Following preliminary hearings a final hearing was held by this court on July 26, 1968 on the plan and on the reports of the Special Master. All the points raised have been both briefed

and orally argued, and the matter is now fully submitted to this, the reorganization court.

In addition to the procedure provided under §77(e), the First Mortgage 4% Bondholders Committee, The Chase Manhattan Bank, Trustee, Manufacturers Hanover Trust Co., Trustee, United States Trust Co., Trustee, and Oscar Gruss & Son (hereinafter collectively referred to as "the bondholders") appealed to a three-judge court in the Southern District of New York under Title 28 U.S.C. §2284 on the ground that the terms and conditions of the inclusion of the New Haven in the Penn-Central under the plan were not just and reasonable, or equitable, as required by §§5(2)(b) and (d) of the Interstate Commerce Act. That court, consisting of Circuit Judge Friendly and District Judges Weinfeld and Levet, heard the case and later filed its decision July 10, 1968 (S.D.N.Y. 68 Civ. 296). Many of the issues raised in the three-judge court are also before this court and, where the three-judge court did not adopt the position urged by one of the parties, that party has in most instances renewed its claim here by attacking the rationale of the three-judge court in deciding such issues. That court remanded the case to the Commission for further proceedings consistent with its opinion; and, in conformity with the views of all parties, this court likewise refers the proceedings back to the Commission for further action. In so doing this court intends to leave the Commission the maximum flexibility of decision within the general guidelines set by this court and the three-judge court.

The two principal questions now before the reorganization court are: (1) whether or not the standard of value which the New Haven is entitled to receive for the transfer of its assets to the Penn-Central is its liquidation value as of December 31, 1966 or some other measure of worth, together with the accompanying question of whether the Commission conformed to the proper standard in its order of November 16, 1967; and (2) whether the time is now foreseeable in the near future when the continued deficit operation of the New Haven in the public interest at the expense of the creditors must be held to be a taking of their property without due process or just compensation, in violation of the Fifth Amendment to the Federal Constitution.

Before discussing these major points further mention should be made of the general constitutional principles which bear on their solution. While the power provided under the Bankruptcy Act is broad and ample,[2] the Constitution places limits on the exercise of that power by both Congress[3] and the courts.[4] The due process clause of the Fifth Amendment, for example, protects the rights of creditors from unlawful invasion by either Congress or the courts.[5] As the rights of creditors cannot be arbitrarily sacrificed or restricted, the creditors of the New Haven are entitled to a constitutional minimum of value for the property to be sold to the Penn-Central, which, on its part, is entitled to be required to meet only equitable terms. The constitutional and equitable principles, however, are sufficiently flexible that a proper value may be arrived at which is fair to all parties. This court is of the opinion that it faces an even more serious problem which is the continuing and accelerating wasting away of the Debtor's estate through operating losses while the legal processes for determining value go on and the consummation of actual inclusion is deferred.

In expressing its own view concerning the proper standard of valuation it should still be borne in mind that the court does so primarily to furnish a guideline; and in making its own determination the Commission should make all necessary findings relevant, not only to that standard, but also those essential to such other theory of price determination as the Commission may adopt if it is in disagreement with the liquidation measure of valuation. It is the opinion of the court that the Penn-Central should pay to the Trustees of the New Haven at least the liquidation value of the New Haven as of December 31, 1966. This is so not because the Constitution necessarily requires it but because that standard, under the circumstances of this case, is fair both to the creditors and to the Penn-Central.

Some of the parties have asked the court to reject this standard and argue in favor of a "going concern value" while others seek the adoption of a "fair upset value," but these proposed alternatives are wholly inappropriate for the attendant conditions of the present reorganization. The concept of "going concern

value" is fictional as applied to the New Haven because it ignores the Railroad's long and continuous history of deficit operations." Indeed, as later noted herein the New Haven's operations must soon terminate. With regard to "fair upset value" it is difficult to see how, in applying it to the New Haven under the circumstances of the reorganization, it would differ at all from "fair liquidation value." The term "fair upset price" in its ordinary meaning refers to the lowest price which would be accepted for an item offered for sale at an auction. From this beginning it was borrowed and used extensively in equity reorganizations which were designed to recapitalize a viable corporation which had operating income,[7] and in this connection was used to force minority security holders into accepting the plan. In other instances the upset price was fixed for the purpose of protecting such minority interests. In any event, it was principally used against co-security holders rather than against a third party such as Penn-Central.[8] In connection with a corporation as moribund as the New Haven, fair upset price is analogous to "fair market" or "liquidation" value, although there is some authority that it may be less, at least where the purchaser is a public authority.[9]

Turning to a somewhat fuller discussion of liquidation value we start with the bondholders' argument that the value fixed as of December 31, 1966 must be treated as a fixed and immutable constitutional minimum which cannot be diminished by subsequent deficit operation of the Railroad. Both the Commission and the courts, however, have reiterated in this and in related proceedings that as bondholders of a railroad their interests are subject to such invasion as may be essential to continue the operation of the railroad for a reasonable period of time to provide an opportunity to work out a permanent plan or means of continuing the operation, if possible, to the extent that it is required by the public interest.[10]

Throughout the reorganization proceedings the parties, the Trustees and the court have been aware of the duty and necessity resting upon the Trustees to preserve the assets of the Debtor's estate for the creditors on the one hand, and, on the other hand, the obligation in the public interest, to keep the Railroad going,

even as a deficit operation. For a time this dichotomy of purposes ran in parallel, but before long they began to assume collision courses. A brief resume of the history may be helpful.

The petition for reorganization in this case was filed on July 7, 1961. The immediate problem of the Trustees was to stem the the cash loss, then flowing out at the rate of $1,500,000 per month. By increasing the efficiency of operation, imposing strict economies and deferring certain payments this cash loss was arrested in 1962, although cash attrition began again to present a problem in 1964.[11] At first it was thought possible that the Railroad might operate as a carrier of freight only or with greatly reduced passenger service. There was also a flurry of interest by the four States concerned and the federal Government which raised the hope that sufficient grants would be provided to enable the Railroad to operate on a break-even basis. But, except for full tax relief and substantial grants by Connecticut and partial tax relief and smaller grants by New York, and Rhode Island, no subsidies or prospects of subsidies of a size sufficient to make up for the operational losses were forthcoming. The gains achieved by the Trustees were soon wiped out by a series of increases in wages, increased cost of materials, equipment and supplies and severe competition from trucks, automobiles, planes and sea borne traffic. Meanwhile, an application of the Pennsylvania and New York Central Railroads to merge was filed on March 9, 1962. Consistently with the Trustees' previously held opinion that a merger with a large trunk line railroad would be the most promising and feasible means of continuing the viability of the New Haven's transportation system, they at once sought inclusion, in a merged Penn-Central system.[12] Before the Commission had acted they also, forehandedly negotiated a contract with the Pennsylvania and New York Central for the inclusion of the New Haven in a merged Penn-Central to protect the New Haven in the event that the Commission did not require the inclusion as a condition of the merger.[13] While the preservation of the New Haven was not the sole justification for the approval of the Penn-Central merger, this promising solution for the very difficult New Haven problem, demanded by the public interest, was undoubtedly a make-weight

which has a definite effect on tipping the balance in favor of the approval of the merger. It was about the only enducement which could bring Pennsylvania and New York Central to make such an agreement with the New Haven.

By about 1963 it became apparent that the inclusion of the New Haven in the Penn-Central merger was the only salvation for the New Haven as an operating railroad, and at that time it was thought to be the solution which best served the interests of the creditors as well as the public interest. But by March 27, 1967, when the Supreme Court remanded the Penn-Central case to the Commission, after the merger with the inclusion of the New Haven had been approved by the Commission and appealed,[14] Oscar Gruss and Son and the First Mortgage Bondholders Committee *concluded that the operating losses of the New Haven were* eating away the assets of the Railroad or building up superior liens on those assets to the point where their opportunity to recover something on their own bonds would best be realized by liquidation.[15] Even after the approval by the Supreme Court, on January 15, 1968, of the Penn-Central merger and the inclusion therein of the New Haven,[16] these bondholders continued to press their motion to liquidate. Their petitions were rejected by this court on February 13, 1968.[17] At that time the first step in the plan of reorganization had been approved by the Commission, although it had not been certified to the reorganization court. It was anticipated that review of the plan by a three-judge court and by this court, with any appeal to the Court of Appeals from this court's judgment, would be given high priority, and appeals to the Supreme Court from both cases would be docketed with the Supreme Court at the opening of the October, 1968 term. Accordingly, although it was clear that the liquidation value of the New Haven as of December 31, 1966 was being chiseled down day after day by the operating losses, there was an excellent prospect that the terms of the transfer and the amounts to be paid or assumed by the Penn-Central for the assets of the New Haven would soon be fully adjudicated. As investors in railroad bonds, the petitioners were required in the public interest to suffer the burden of keeping the Railroad operational for a reasonable period

to permit this to be accomplished.[18] As mentioned in the opinion denying the petition, it was unthinkable to terminate the reorganization proceedings, after a long and hazardous journey through a dark and seemingly endless tunnel just as light began to show at the far end.[19] Now the circumstances have changed very radically. Unfortunately the plan must be referred back to the Commission for further proceedings, which at best will probably and unavoidably be very time consuming. At the hearing on the plan Attorney Auerbach, speaking for the Trustees of the New Haven, stated that it would not be possible for judicial review proceedings to reach the Supreme Court before the October, 1969 term. This statement was neither contradicted nor challenged. The tunnel has lengthened and the light is no longer bright. Moreover, most serious of all is the fact that the New Haven Railroad no longer has the capability to reach the far end of the tunnel, and, as more fully discussed below, there is an urgent necessity that the New Haven be included in the Penn-Central at an early date. The following tables provide compelling evidence of the history and trend of the Railroads' financial plight and of the pending crisis.

In Appendix D of its report and order of November 16, 1967, the Commission set forth New Haven's deficits for the years 1961-1966 as follows:

The New York, New Haven and Hartford Railroad Company
condensed income statement for the years 1961-66

Year	Net Railway oper. deficit	Income (deficit) before fixed charges	Net Inc. (deficit) after fix. chgs. and other deducs.
1961	($19,577,000)	($11,952,000)	($19,500,000)
1962	(11,514,000)	(5,083,000)[20]	(12,741,000)
1963	(10,090,000)	(4,884,000)	(12,264,000)
1964	(17,056,000)	(8,326,000)	(15,263,000)
1965	(16,008,000)	(8,422,000)	(15,063,000)
1966	(13,044,000)	(5,359,000)	(11,345,000)

Comparable deficits for the period from December 31, 1966 through June 30, 1968 follow:[21]

Year	Net Railway oper. deficit	Income (deficit) before fixed charges	Net Inc. (deficit) after fix. chgs. and other deducs.
1967	($20,179,000)	($13,720,000)	($19,514,000)
	Six months ended June 30, 1968		
	(12,190,000)	(8,494,000)	(11,420,000)

The rate of cash loss for 1967 and the first seven months of 1968 follows:

	1967	1968
January	($ 997,000)	($1,907,000)
February	(1,766,000)	(89,000)
March	799,000	(659,000)
April	(291,000)	(937,000)
May	(713,000)	(1,146,000)
June	(537,000)	(1,699,000)
July	(1,876,000)	(886,000)
August	13,000	
September	517,000	
October	(377,000)	
November	(296,000)	
December	508,000	
	($5,016,000)	($7,323,000)

The New Haven's cash losses are now being made up out of borrowings under Order #480, dated December 19, 1967 in which this court authorized the Trustees to borrow up to $25,000,000 from the Penn-Central. The Trustees stated at the hearing on the reorganization plan that this amount would not carry the Railroad beyond June 1969 — an estimate which is likely to prove optimistic. In any event, this court now concludes that such borrowing to carry the deficit operation beyond the end of 1968 is not justified. Order #480 is being modified accordingly. In addition, no funds now in the registry of the court, held in lieu of mortgaged property which has been sold, will be used to pay operating losses.

There remains, of course, the public interest in keeping the New Haven going, and the bondholders may be required to bear

their share of the losses to December 31, 1968 subject to such loss sharing by Penn-Central as the Commission may direct, to afford the Commission an opportunity to consider and rule upon the issuance of an order to the Penn-Central physically to take over and commence operating the New Haven Railroad not later than January 1, 1969, leaving the price and the other terms of the inclusion to be determined later.[22]

If the Commission decides not to issue such an order this court will reluctantly be forced to entertain a motion to dismiss the reorganization proceedings. §§77(e) and (g). While liquidation will have to await authority to abandon, the trains will stop in January because, with no money with which to pay employees, suppliers and materialmen, actual operation of the Railroad will cease.

The extent to which the constitutional minimum of value of property rights to which the bondholders are entitled (in this case the liquidation value as of December 31, 1966) may properly be invaded in the public interest to keep railroad operations going pending a solution of the problem of reorganization, is hardly a matter which can be determined with mathematical precision. It involves a consideration of the amount and nature of the Railroad's obligations, the seriousness of adverse consequences to the public if service were terminated, the rate of losses and the feasibility of possible solutions. In view of the history of this deficit operation from the time of the filing of the petition under §77 and even before, the size of the losses, the long period of time necessarily involved in seeking to work out a solution, short of liquidation, through inclusion in the Penn-Central, the present condition of the Railroad and the rate of loss and out-flow of cash in the recent past and in the foreseeable future, this court finds that the continued erosion of the Debtor's estate from operational losses after the end of 1968 will clearly constitute a taking of the Debtor's property and consequently the interests of the bondholders, without just compensation. It is therefore constitutionally impermissible, and obviously no reorganization plan which calls for such a taking can be approved.

Two of the several cases cited elsewhere in the footnotes may usefully be summarized in support of this conclusion:

In *Continental Illinois National Bank & Trust Co.* v. *Chicago, Rock Island & Pacific Ry. Co.*, 294 U.S. 648, 658, 677, 684, 685 (1935), the Supreme Court sustained an order of the bankruptcy court enjoining creditors who held collateral notes from selling the collateral despite the possibility of a decline in its value during the period of restraint. Noting that the value of the collateral greatly exceeded the secured indebtedness and that the order contemplated only reasonable delay, the Court nevertheless suggested that the order would have to be reconsidered if injury to the creditors became irreparable through an unreasonably long delay in the proceedings before the bankruptcy court. *See also In re Brown*, 84 F.2d 433, 436 (7 Cir. 1936) (injunction against sale of collateral sustained, without prejudice to renewed application if the fact situation changes so that prejudice to the creditor is shown). In *In re third Ave. Transit Corp.*, 198 F.2d 703, 707 (2 Cir. 1952), the Court of Appeals reversed an order directing the first mortgage indenture trustee to turn over certain sums to the reorganization trustees in return for certificates of indebtedness bearing interest but without maturity date. The court declared that such involuntary loans could not be ordered unless there was a high degree of likelihood that the debtor could be reorganized within a reasonable time with no injury to the secured creditors who were being forced to advance the money. Acknowledging that the judge properly took into account the public interest in the debtor's continued operations, the court nevertheless advised that there are "strict limits to the extent to which, in reorganization proceedings, the interests of creditors . . . may be sacrificed to the public interest; to exceed those limits is (to say the least) to come dangerously close to the edge of unconstitutional taking of property, a line from which courts should keep away if possible."

There is presently no reason why the Penn-Central should not take over the New Haven at the beginning of 1969. The record of the merger and inclusion cases make it abundantly clear that the inclusion of the New Haven was an absolute and unequivocal

condition of the approval of the merger of the Pennsylvania and New York Central Railroads, from the order of the Commission through the decision of the Supreme Court. In consummating the merger Penn-Central agreed to pay whatever price and submit to whatever terms for the inclusion that the Commission and the Courts might find reasonable. Counsel for Penn-Central in arguing the merger case before the Supreme Court, in response to questions from the bench, made this perfectly plain.

> "Mr. Cox The order [in] which the Commission did this was an order made in the New Haven Inclusion Case and, of course, which can be and undoubtedly will be reviewed before the three-judge court in the usual way and as Mr. Auerbach points out, of course, it is upon that view that the Commission ordered.
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> The Commission has to fix terms that are more onerous on the Penn-Central, the Penn-Central having consummated the merger as allowed to do in the meantime, would be bound by those conditions as a result of the Commission's original order."
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> "Mr JUSTICE BRENNAN. I take it Penn-Central's judgment must be there are other values, even if it is a losing operation, a merger which makes the merger overall in their best interest; is that it?
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> Mr. Cox. The answer is yes. They won't be prepared to go forward with it unless —
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> Mr. JUSTICE BRENNAN. As I understand it, whatever this arrangement is now, Penn-Central can't get out of it.
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> Mr. Cox. They can't get out of it if they consummate the merger.
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> Mr. JUSTICE BRENNAN. If the merger is approved, it must go forward and whatever the result, Penn-Central will be stuck with it; is that it?
>
> Mr. Cox. They would be stuck with it in this sense.

Mr JUSTICE BRENNAN. Suppose a review of this recent order of ICC, and it could happen, I expect, the Commission might be reversed, and they go back to the Commission for something else, something better perhaps, what is Penn-Centrals' position then?

Mr. Cox. I understand, having consummated the merger, of Penn-Central, you have two companies involved by that act to be bound by any conditions the Commission fixed originally or on remand, under Section 5(2)(d) of the Act, insofar as the New Haven is concerned. . . ."

(Transcript pp. 136, 144-145).

No question remains in the case as to whether or not the Penn-Central has the obligation to include the New Haven. Any claim that this is an issue which the Commission may still pass upon and sustain or deny is untenable. The only related questions remaining are when and at what price. But the time of actual inclusion is not dependent upon the prior fixing of the price and the terms. In his separate opinion in the decision of the three-judge court, Judge Weinfeld took the position that because the inclusion of the New Haven was a condition of the Penn-Central merger, the New Haven should have become a unit of the Penn-Central merger, "with the latter necessarily absorbing operating losses from the date of the merger." He recognized that, as a practical matter, actual inclusion coincidental with the merger would have been impossibly difficult. But the only reason for this was the complexity of putting together two of the largest trunk line railroads in the country to form the largest railway system in the world. This circumstance called for a postponement of the physical inclusion of the New Haven which carried with it sizeable problems of its own. The acute stage of welding the Pennsylvania and the New York Central systems into one operation is sufficiently advanced, however, so that the reason for delay in absorbing the New Haven no longer obtains. As this was largely for the benefit of the Penn-Central, the cogency of what Judge Weinfeld said is apparent.

It may well be argued that the Commission and the Courts, including the Supreme Court, by approving the merger conditioned upon the inclusion of the New Haven, placed the responsibility on the Penn-Central for bearing the losses in the public interest, and thereby relieved the bondholders of that obligation. It will, however, rest within the judgment of the Commission on remand to decide whether all or only a portion of the losses of the New Haven should fairly be borne by the Penn-Central for the period February 1 to December 31, 1968.

Before turning to specific items in the valuation it should be noted that the Commission was, indeed, faced with many novel and difficult problems. Some of the errors in the Commission's report were due undoubtedly to oversight, caused by the sheer complexity and quantity of the evidence and the claims relating to the factual and legal issues, as well as the formidable task of synthesizing them into findings and conclusions under the urgency and pressure of the shortest possible span of time. On the question of the Grand Central properties the Commission suffered from a paucity of evidence and legal sources for an interpretation of the claims of the parties in interest.

In any event, the court is keenly aware that it is easier from a more detached position to note errors in a plan than it is to formulate one in the first place. Most of the specific claims of error in the reorganization plan which necessitate its remand to the Commission are discussed in the excellent opinion by Judge Friendly, writing for the three-judge court. The reorganization court will, therefore, confine its discussion to matters which it wishes to enlarge upon, qualify or explore along somewhat different lines. There has already been discussed liquidation value as the proper standard, but no purpose would be served by traversing again all areas of agreement. The points not to be discussed, on which both courts are in agreement, however, will, for convenience, simply be identified as follows:

Those concerning the valuation of the New Haven:

(a) the Commission's failure to discount expenses of liquidation;

(b) the under valuation of $1.1 million of the New Haven's interest in the Boston & Providence R. R. Corporation;

(c) the refusal by the Commission to consider possible tax benefits to Penn-Central;

(d) the rejection of the testimony of bondholders' expert, Wyer, concerning the minimization of the expenses of liquidation as to portions of the Railroad's lines which might be taken over by other carriers; and

(e) the acceptance of the Commission's conclusions as to the value of passenger cars and of investments by the New Haven in Fruit Growers Express, New York Connecting R. R., Pullman Co., Railway Express Agency and certain affiliated lines; also the Commission's finding of values through "rounding off."

Those concerning the value of the consideration to be received:

(f) the Commission's failure to take into account that $16.2 million of the price may have to be expended to pay off prior tax liens in order that the properties may be sold free and clear of such liens;

(g) approval of the Commission's valuation of the Penn-Central stock at $87.50 per share, based upon its own calculation of the estimated future earning power of Penn-Central and upon the testimony of Trustee Kirk, a well qualified expert. There is no reason why recent fluctuations in the market value of these shares should change the disposition of the matter;

(h) the failure of the Commission to discount the Penn-Central bonds which Penn-Central had the option to use in satisfaction of its "Purchase Price Adjustment" provisions; and

(i) the necessity for re-examination by the Commission of bases for differences between its calculated liquidation value and the value of the consideration to be received from Penn-Central.

Cost of acquisition to Penn-Central:

(j) Commission's errors in valuation of 23 million principal amount of Penn-Central 5% bonds and assumption by the Penn-Central of Boston & Providence mortgage as well as those used in Purchase Price Adjustments; and

(k) necessity for reconsideration of cost of assuming equipment obligations.

The Reorganization Court concurs in and adopts the reasoning, conclusions and the dispositions relating to the foregoing matters, made by the three-judge court, and concludes that they require the remand of the Commission's plan by the Reorganization Court.

It now turns to other subjects dealt with in the Commission's report which call for brief discussion.

1. *The New Haven's Interest in Grand Central Terminal (G.C.T.) Properties.*

The nature and extent of the legal interest of the New Haven Railroad in the G.C.T. properties constitutes the most important and most difficult problem in determining a fair valuation of the Debtor's assets. In the absence of a final adjudication of what those interests are, through a plenary suit in the courts of the State of New York, the Commission had to estimate the value of New Haven's claim. The Trustees of the Railroad did not go forward with a plenary suit because they had been advised by competent and experienced counsel that, on liquidation of the New Haven with none of its cars moving in and out of the Grand Central, the New Haven would have no interest in the G.C.T. properties, save for the repayment of certain building advances. In the light of this they felt it would be a dereliction of their duties to risk the tremendous expense and long delay of four to five years, during which, because of New York Central's and later Penn-Central's opposition to treating the G.C.T. property claims as separate from the rest of the merger and inclusion, all proceedings would have been held up for a time longer than the New Haven could survive. The Commission in its report con-

cluded that " . . . the claims of New Haven are not frivolous but claims of substance and, in the absence of litigating them, they must be deemed to be valuable."

The means adopted by the Commission to determine the extent and worth of the New Haven's claims, however, were altogether too imperfect to be sustained. Part of the Commission's difficulty stemmed from its limited concept of the extent and nature of New Haven's interests in the properties. This court, as an aid to itself, in reviewing the fairness and equitability of the Commission's decision, appointed the Special Master to "make a legal appraisal of the interests and rights of the Debtor in said properties, including the nature of the Debtor's interest in the event of the cessation of passenger operations in the Grand Central Terminal." Judge Van Voorhis had just retired as a Judge of the Court of Appeals of the State of New York after a distinguished career on that and the two next highest courts of the State. His thorough and illuminating reports, filed with this court, in broad aspect cover two areas: the first is a description of the nature of the legal interests of the New Haven in the G.C.T. properties, which this court accepts, adopts and incorporates by reference as a part of this opinion; the second is a survey of the evidentiary terrain, disclosing the existence and availability of proof, on the basis of which dollar value may be computed. The purpose of the latter was to discover whether there was anything beside a theoretical reason for remanding the Commission's plan. If, as a practical matter, full recognition of all of the legal interests the New Haven could properly claim would, at best, lead to no more than the 13 million dollars the Commission estimated to be the value of the claims, it would be a waste of time to remand on this issue. The purpose of the survey of the terrain was, therefore, strictly limited as an aid to this court in determining whether or not the value found by the I.C.C. was fair and equitable and it was in no sense intended to be a new finding of value, which lies in the sole province of the Commission. *Ecker* vs. *Western Pacific R. Corp.*, 318 U.S. 448, 477 (1943).

The Special Master's reports show that there is evidence available to show a value considerably in excess of the Commission's

appraisal of the claims, and it therefore must be concluded that the $13,000,000, found by the Commission, is neither fair nor equitable. The conclusions of the three-judge court are strikingly similar to those of the Special Master.

As the situation now stands, the Commission, the three-judge court, and this court have concluded that the New Haven has valuable rights in the G.C.T. properties that would survive the cessation of operations by the New Haven. While this consensus does not establish New Haven's rights with the same finality as an adjudication by the New York state courts would do, the Commission should proceed, as it did before, on the basis that the New Haven's rights are valuable. In appraising the value of the claims, the Commission may, of course, take into consideration the fact that there has been no such adjudication.

In addition, it is suggested that the Commission consider and make findings as to what value, if any, attaches to New Haven's present right to share in the income for the purpose of defraying its cost of operating in and out of the terminal. Whether an authority will take over New Haven's commuter operations and succeed to this right, which the New Haven now has, or Penn-Central succeeds to that right, a valuable interest will have been acquired. There is admittedly a certain element of speculation involved, and the Commission would, if it concludes that this present right has value, be justified in adopting a somewhat higher capitalization rate than 8%.

The only remaining comment concerns New Haven's 50% interest in the excess income in the Terminal Account and, that is, that the period considered should commence with the 1964 account and run to the time of New Haven's inclusion in Penn-Central.

2. *Harlem River and Oak Point Freight Yards.*

The three-judge court concluded that the Commission's report on the valuation of these properties did not adequately explain its basis for rejecting the higher of the two appraisals submitted on

behalf of the Trustees or the appraisal for industrial use made by the bondholders' expert. It also raised the question whether or not the deductions from value made in the course of the appraisal which the Commission accepted was not duplicated by the deductions made by the Commission in its overall calculations. While a clarification of these matters is desirable, it appears to this court on the present record that there was substantial evidence to support the Commission's valuation and not enough to show that it was unfair or inequitable.

3. *Claim of the Trustee of the Harlem River Division Mortgage for Assumption.*

The three-judge court declined to pass upon this claim and left it to be dealt with by the Reorganization Court. The Harlem River mortgage is fully secured; it is relatively small in amount — $6,647,000; it carries a low interest rate of 4½% [sic] and matures in January, 1963. The accrued and unpaid interest as of the end of 1968 will total approximately $2,260,000. It is reasonably certain that the consideration to be paid by Penn-Central to the New Haven will be increased by an amount in excess of the principal and accrued interest on the Harlem River Mortgage. The present plan leaves the way open for the mortgagees to lose their lien and to be required to accept in its place security of less quality. This would damage the Harlem bondholders without contributing anything really necessary for the reorganization. Under the circumstances this would be unfair and inequitable. To prevent any undue burden falling on the Penn-Central in this regard, the Commission could provide for Penn-Central's assumption of the mortgage subject to some possible modifications. For example, if Penn-Central's inclusion of the New Haven takes place on January 1, 1969, it could then assume the Harlem River mortgage, subject to such qualifications in its favor as elimination of any sinking fund requirements and an option to pay the accrued interest in four or five installments over the remaining life of the mortgage.

4. *Loss Sharing Formula*

The three-judge court's opinion dealt with this subject in detail and concluded that the formula was improper because the provision for the downward percentage of Penn-Central's share of losses over the three ensuing years was designed to curtail litigation by the bondholders. The reorganization court must take general responsibility for suggesting this kind of provision. It has been recognized by most courts, including the Supreme Court, that litigation may be used not only for the fair determination of disputed claims but as a tactical or strategic weapon in itself. In this case the measure may have reflected an ill-founded fear on the part of the court. It is certainly true that Penn-Central could equally well seize an opportunity to delay and any necessary steps designed to prevent that kind of thing should apply to all of the parties. This should in no way reflect on counsel for any of the parties whose decorous advocacy and outstanding professional skill have been manifest throughout. The issues raised both before the three-judge court and before this court have become almost academic in view of the necessity for the inclusion of the New Haven in Penn-Central by January 1, 1969. The Commission must decide whether to order such inclusion and what share of the losses from February 1, 1968, the date of the merger, to the end of 1968 should be borne by Penn-Central. This court is of the opinion that, as mentioned above, it should be a substantial percentage. Present circumstances also render academic the claim that the Commission should prescribe Appendix G type conditions for the protection of the New Haven.

5. *The Providence-Worcester*

The Commission reserved jurisdiction to pass upon Providence & Worcester's requests arising out of amendment #1 to the New Haven's plan of reorganization rejecting the lease with that road. Counsel for Providence & Worcester appeared at the hearing held by this court and asked the court to order the Commission to require the assumption of the lease by Penn-Central at the time of the inclusion. But no reason was given which persuaded the

court to interfere with the Commission's reservation of jurisdiction or the Commission's discretion to pass upon the issue at a later time.

6. *Effect of Correction of Errors in Consideration to be Paid.*

The flexibility left to the Commission in its consideration on remand of the matters discussed in the opinion of this court and that of the three-judge court will result in an addition to the consideration to be paid by Penn-Central to the New Haven under the terms of the Commission's plan now on review in an amount which may properly fall within a range of $33,000,000 to $55,000,000. It is the present opinion of the court that amounts below this range would be unfair and inequitable to the creditors and an amount in excess of this range would appear to be unfair and inequitable to Penn-Central.

Other points raised by the parties, such as Penn-Central's argument that these proceedings cannot be held to be in effect a condemnation and the bondholders' claim that the Commission erred in basing its plan in large part on the Trustees' plan which closely followed the terms of the inclusion agreement between the New Haven Trustees and the Pennsylvania and New York Central Railroads, require no discussion. The Trustees' plan has not been reduced to little or no significance by the action taken by the reviewing courts. On the contrary, it still furnishes a sound, constructive and proper nucleus for the Commission's disposition of the case on remand. What it needs is supplementation rather than repudiation.

The three-judge court found that the total cost of acquisition of the New Haven to Penn-Central will be something in excess of $250 million. Judge Friendly reached this amount by capitalizing at 8% estimated future annual losses of 8.5 million, which added $106 million to other items of cost. Judge Weinfeld, however, disagreed with the addition of this sum, and Judge Levet felt that consideration of the subject of cost to Penn-Central was unnecessary under the theory adopted by the Commission. Judge Friendly went a long way toward eliminating the significance of the ad-

dition made to cost by pointing out that, even after allowing for New Haven losses, Penn-Central would ultimately save $72.5 million dollars per annum which capitalizes at $900 million.

Once it is decided that the New Haven creditors have contributed in losses all they can constitutionally be required to dedicate to the pulbic interest, the responsibility for future losses becomes an issue between the Commission and Penn-Central. As the bondholders point out, it is the Commission which is compelling the continued operation of the heavily deficit ridden passenger services and losing freight operations. The creditors cannot very well be faulted or penalized for this. Surely it is not contemplated that Penn-Central is immune from assuming, in the public interest, operational losses of the New Haven. The whole purpose of making the inclusion of the New Haven a condition of the merger was to require Penn-Central, which, in being permitted to merge, was granted the opportunity to realize tremendous economic benefits, to take over and operate a helplessly sick but still needed railroad, which it could well afford to do. It is part of the price Penn-Central is called upon to pay for the right to merge. The right to merge was granted, the merger has taken place, and the price should be paid.

> "Continuation of the operations of the NH, which the Commission has found to be essential, can be assured only upon and after effectuation of the merger of the Penn-Central. The bondholders agree that to delay the Penn-Central merger until all proceedings necessary to include the NH have taken place may well mean the end of NH operations. The only realistic way to avoid this is to permit prompt consummation of the Penn-Central merger subject to appropriate conditions respecting the New Haven which Penn-Central will perforce accept by its act of merger. . . ."

Penn-Central Merger and N & W Inclusion Cases, 389 U. S. 486, 510 (1968).

In conclusion this court proposes that the Commission consider first the matter of the inclusion order and with it a partial payment of the purchase price.

In its order of November 16, 1967, the Commission found the consideration agreed to between the Trustees and the merging railroads fair; both the three-judge court and this court have concluded that the consideration was too low. While the upward adjustment remains to be determined, the Commission could properly provide for a partial payment with an order for inclusion to take effect January 1, 1969. For example, it could appropriately require Penn-Central to deliver 950,000 shares of its stock, $23,000,000 principal amount of its 5% bonds and pay $8,000,000 in cash. It is also suggested that the matters of early inclusion and partial payments, which are extremely urgent and severable from the other issues in the case, be considered first and as expeditiously as possible.

The case is referred back to the Commission for further proceedings including the modification of the plan in accordance with this opinion.

Dated at New Haven, Connecticut, this 10th day of August, A.D. 1968.

ROBERT P. ANDERSON
United States Circuit Judge,
sitting by designation.

Footnotes:

[1] Pennsylvania R. R. — Merger — New York Central R. R., 331 I.C.C. 643 (1967).

[2] 1 Collier, Bankruptcy, ¶ 0.02 at 5 (14th ed. 1968.)

[3] Louisville Joint Stock Land Bank v. Radford, 295 U.S. 555 (1935) (Federal Frazier-Lemke Act of 1934 violated due process clause of Fifth Amendment). The amendatory act of 1935 was thereafter sustained as constitutional. Wright v. Vinton Branch of Mountain Trust Bank, 300 U.S. 440 (1937). *See also* Ashton v. Cameron County Water Improvement Dist. No. One, 298 U.S. 513 (1936) (Municipal Debt Readjustment Act was an unconstitutional infringement on state sovereignty). The constitutionality of the second Municipal Debt Readjustment Act was sustained in United States v. Bekins, 304 U.S. 27 (1938).

[4] Continental Ill. Nat'l Bank & Trust Co. v. Chicago, Rock Island & Pac. Ry. Co., 294 U.S. 648 (1935).

[5] See Louisville Joint Stock Land Bank v. Radford, *supra*, note 3; Continental Ill. Nat'l Bank & Trust Co. v. Chicago, Rock Island & Pac. Ry. Co., *supra*, note 4.

[6] The last year in which New Haven realized any net railway operating income was 1957. Since that time the deficit in net railway operating income has varied from a low of $3,855,547 in 1958 to a high of $20,179,000 in 1967. See Petition for Order No. 404, Printed Record pp. 4443, 4446, New York, N. H. & H. R. Co. Discontinuance of Trains, 327 I.C.C. 151, 166 (1966), and Pennsylvania R.R. — Merger — New York Central R.R., 331 I.C.C. 643 (1967), Appendix D and *infra* in the text.

[7] *See, e.g.*, Glenn, Liquidations §433 at 611; 6 Collier ¶ 0.04 [2.2]; 4 Moore, Federal Practice, (2d ed.) ¶ 24.11.

[8] 6 Collier, Bankruptcy, ¶ 0.04 [2.2]; 15 Fletcher, Private Corp., §7272, n. 58 (perm. ed. rev. 1961).

In foreclosure sales, particularly in the case of railroad mortgages, the real bidder at the sale was usually the holder of the majority interest in the bonds. Since he would be allowed to pay off a percentage of his bid in bonds it was to the majority holder's interest to bid as low as possible. Under these circumstances it was necessary for the protection of minority interests to have the court set a minimum price below which no sale would be confirmed. This was the "upset price." Glenn, Liquidations §433, at 611; Guaranty Trust Co. v. Chicago, M. & St. P. Rwy., (E.D. Ill. 1926) 15 F.2d 434.

Several bases for establishing upset price are discussed in II *Bonbright, Valuation of Property*, p. 850, and in *Weiner, Conflicting Functions of the Upset Price*, 27 Colum. L. Rev. 132, 139 (1927).

[9] New York Trust Co. v. Portsmouth & Exeter St. Rwy., 192 Fed. 728 (C.C.D. N. H. 1911); 2 Gerdes, Corporate Reorganizations, §1062 (1936 ed.); 7 Fletcher, Private Corporations, §3290 at 447 (perm. ed. rev. vol. 1964).

[10] Pennsylvania R.R. — Merger — New York Central R.R., 331 I.C.C. 643, 704; Penn Central Merger and N. & W. Inclusion Cases, 389 U.S. 486 (1968); *cf.* In Re Third Ave. Transit Corp., 198 F.2d 703, 707 (2 Cir. 1952).

[11] See Petition for Order No. 404, Printed Record, pp. 4443, 4449.

[12] See Petition for Order No. 109, Printed Record, p. 927.

[13] This contract was never brought before the Reorganization Court for approval or disapproval, but it furnished the basis for the Trustees' plan submitted to the Commission which adopted portions of it in formulating its own plan.

[14] Baltimore & O. R.R. v. United States, 386 U.S. 372 (1967).

[15] See Answer of First Mortgage 4% Bondholders Committee to the Trustees' Petition for Instructions (Order No. 441) and Cross-Petition for Termination of Reorganization Proceedings, Printed Record 5087; Answer of Oscar Gruss & Son to Petition of the Trustees for Order No. 441, Printed Record 5121.

[16] Penn Central Merger and N. & W. Inclusion Cases, *supra*, note 10.

[17] Memorandum of Decision on Petition for Order No. 441; Cross-Petitions of First Mortgage Bondholders Committee and of Oscar Gruss & Son for Termination of Reorganization Proceedings, and Trustees' Motions to Dismiss the Cross-Petitions, Printed Record 5633.

[18] See *supra*, note 10.

[19] Printed Record pp. 5633, 5638.

[20] Pennsylvania R.R. — Merger — New York Central R.R., 331 I.C.C. 643 (1967), Appendix D contains a typographical error showing this figure as 55,083,000.

[21] Source — Rail Form A for the year ended December 31, 1967 — The New York, New Haven and Hartford Railroad Company, and, I.C.C. quarterly report Form IBS, 2nd quarter 1968.

[22] Immediate inclusion has been sought by Oscar Gruss & Son since the latter part of 1966; and there is being considered in connection with the hearing on the Reorganization Plan, a motion by the State of Connecticut for immediate inclusion.

IN THE

UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF CONNECTICUT

In Proceedings for the Reorganization of a Railroad

In the Matter of
THE NEW YORK, NEW HAVEN AND HARTFORD RAILROAD COMPANY,
Debtor.

No. 30226

ORDER DISAPPROVING THE FIRST STEP OF THE PLAN OF REORGANIZATION OF THE DEBTOR AND REFERRING THE PROCEEDING BACK TO THE INTERSTATE COMMERCE COMMISSION FOR FURTHER ACTION

The first step of the Plan of Reorganization having heretofore been certified to the Court by the Interstate Commerce Commission, due notice having been given by the Court to all parties in interest of the time within which such parties may file objections to the Plan and their claims for equitable treatment and of the time for hearing said objections and claims, and all parties having been heard or given an opportunity to be heard thereon, and the Court having rendered and filed its opinion stating its conclusions and the reason for its disapproval of the first step of the Plan, now

Orders that the first step of the Plan of Reorganization be and it is hereby disapproved; and in the Court's discretion and on

motion of a party in interest refers the proceedings back to the Interstate Commerce Commission for further action.

The Clerk of this Court is directed to transmit to the Interstate Commerce Commission a copy of all evidence received by the Special Master appointed by this Court to consider the Grand Central Terminal matter, copies of the Report of Special Master Respecting Debtor's Right, Title or Interest in the Grand Central Properties and Supplemental Report of Special Master Respecting Debtor's Right, Title or Interest in the Grand Central Properties, a copy of all evidence received by this Court on the first step of said Plan, a copy of the transcript of hearing in this Court on July 26, 1968, and a copy of this Court's opinion on the first step of said Plan.

Dated: August 12, 1968.

ENTER:

ROBERT P. ANDERSON
United States Circuit Judge,
sitting by designation.

IN THE

UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF CONNECTICUT

In Proceedings for the Reorganization of a Railroad

In the Matter of THE NEW YORK, NEW HAVEN AND HARTFORD RAILROAD COMPANY, Debtor.	No. 30226

MEMORANDUM OF DECISION ON INCLUSION AND PAYMENT BY JANUARY 1, 1969

The Fourth Supplemental Report of the Interstate Commerce Commission, with amended Plan of Reorganization of the New Haven Railroad and Order, was certified to this court on December 2, 1968, in accordance with §77(e) of the Bankruptcy Act. After due notice to all parties in interest, hearings thereon were assigned to commence on December 20, 1968. At the outset the court noted the lack of any appearance by any shareholder, common or preferred, or any holder of a certificate of beneficial interest and declared that all such holders were thereafter barred and foreclosed from asserting any interest in the Debtor's estate because of the I.C.C.'s finding and conclusion, affirmed by the court, that the Debtor was and is insolvent, that the equity of the stockholders and holders of certificates of beneficial interest is valueless, that no provision was or need be made in the plan for payment to them and that submission of the plan to them and a vote by them are not necessary. The court then limited

the issue to be heard on the first day of the hearings to the single question of whether or not the Commission and the court could order inclusion of the New Haven Railroad in the Penn Central and payment by the latter to the former of 145.6 million dollars, which the Commission fixed as a fair and equitable price, without the reviewing court first having fully adjudicated the ultimate price which the Penn Central will be required to pay.

The only party which objects to an order of inclusion and payment of the amount fixed by the Commission, without prejudice to the parties to argue at a later date their claims that the portion of the price in excess of $125,000,000 was too little or too much, is the Penn Central.

It argues that railroad mergers cannot be compelled; they must be voluntary; that in taking over the New Haven it is only a volunteer which agreed to particular terms which were, in essence, that New Haven's inclusion would be upon such fair and equitable terms as the Commission might impose, subject to the approval of this, the Reorganization Court; that the Commission has fixed those terms and, in effect, spelled out Penn Central's contractual obligation and delineated its rights and duties as well as those of the sellers — the Trustees of the New Haven —; and that the Reorganization Court must accept it in full or reject it and remand it to the Commission with a statement of its reasons. It suggests that if the court follows any other course, it would be tantamount to inducing a breach of contract and the imposition upon the Penn Central of terms to which it never agreed.

It also by way of objection takes another but closely related approach, and that is that the Commission's terms in its order are "unitary" and cannot be dealt with on review in a piecemeal fashion. It also asserts that unless there is approval of the plan by the Reorganization Court, the terms of the transfer are not binding on anyone though the Commission contemplated that they should be.

These arguments disclose that Penn Central wants the court to adopt the narrowest conceivable interpretation of its own commitment, the statutes, and the Commission's report and

order. In its role as "volunteer" it forgets that its agreement to include the New Haven was a condition precedent to its own right to merge; that once it did merge, as it did on February 1, 1968, it was "stuck with" taking over the New Haven, even though it was a losing operation, on whatever terms the Commission might find fair and equitable, subject to the approval of the Reorganization Court. In this sense it was an open-end agreement. No one ever suggested that the courts could impose new and different terms on review or that either the Commission or the reviewing courts could or would adopt a standard other than what was fair and reasonable, both to the New Haven and the Penn Central. Penn Central was also aware and agreed that if the courts remanded the case to the Commission for reconsideration, a higher price might result. See opinion of this court of August 13, 1968, 289 F. Supp. 451, 460.

With regard to the claim of a "unitary" concept underlying the plan, particularly with regard to inclusion and final determination of price, it should be noted that the Commission, which made the plan, report and order, repeatedly said that inclusion should not be delayed pending judicial review of price or the reorganization plan, nor does it anywhere hint that if an issue is raised as to the fairness and equitability of the price, the amount fixed by the Commission should not be paid. On the contrary the Commission said:

> "It must be emphasized that by inclusion we contemplate nothing less than a binding transfer to Penn Central, free and clear of all liens and encumbrances, of all the assets of NH proposed to be transferred under the agreement between Penn Central and NH, as amended, *and the concurrent payment to the NH trustees of the consideration which we have here found to be fair and equitable.*"

(Emphasis added.) Pennsylvania Railroad Company-Merger-New York Central Railroad Company, 334 I.C.C. 25, 76 (November 25, 1968). The order itself reflects its clear intention that inclusion and payment be accomplished by January 1, 1969 in spite of the pendency of judicial review. Whether the Re-

organization Court could separate out the issues and deal with them one at a time under Rule 42(b), Fed. R. Civ. P., absent a provision in the Commission's report and order that that course be followed, need not be decided, because in this case the Commission clearly and explicitly so provided. Under the present circumstances of this case, the review of the Commission's plan can only be made in piecemeal fashion. No other way is possible in the light of the emergency faced by the New Haven.

In its opinion of August 13, 1968, *supra*, this court concluded as a matter of law that in view of the tremendous operating losses which had to be absorbed out of the Debtor's assets over the preceding seven years, any further absorbtion of such losses after December 31, 1968 would constitute "a taking of the Debtor's property, and consequently the interests of the bondholders, without just compensation." This court also declared that if the New Haven were not included in the Penn Central by January 1, 1969, the operation of trains on the New Haven lines would cease. None of the basic facts on which this conclusion and consequential declaration rest has been challenged or denied nor has any party or the Commission attacked the correctness and validity of the conclusion.[1]

Stoppage of the trains would, in terms of carrying passengers, result in enormous problems for the passengers themselves and already heavily burdened New York City and the highways leading to it. Approximately 30,000 people in busses or private cars attempting to go into and out of New York every business day would generate difficulties which cannot be contemplated with equanimity. The cessation of freight service would result in a major economic disaster to southern New England. Besides the thousands of Railroad employees who would lose their jobs, other thousands in enterprises dependent on freight service would be put out of work. Immediate inclusion is the only means by which such dire consequences can be avoided.

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[1]Notices of "protective" appeals were timely filed by the bondholders and the Penn Central, but the record has never been docketed and no claimed grounds of appeal have been stated.

Although the Penn Central offers both the carrot and the stick — the carrot by way of an offer to refrain from further appeals or attacks on the Commission's plan and order provided all other parties do likewise and the court, at once, without further hearings adjudges the price to be fair and equitable, and the stick when it darkly suggests that any further remand by the courts which would result in any increase in that price will bring about the necessity for the discontinuance and unscrambling of the merger of the New Haven in the Penn Central —, these are means for persuading the court that it should now declare the price fixed by the Commission to be the ultimate price, cutting off the rights of the bondholders and the States to reply and fully argue part 1 of the plan, and the duty of the court to review it. But there is no basis in fairness or equity to eliminate review by the courts.

It is the court's endeavor to treat the parties as evenhandedly as possible. Obviously the Penn Central is zealous in the interests of its shareholders not to assume any greater obligations than it needs to, and the Bondholders of the New Haven seek to protect their interests in valuable properties of the New Haven, but these considerations need not hold up inclusion. In agreeing to include the New Haven to enhance the likelihood of achieving the Penn Central's own merger, it did not seek an adjudicated purchase price and a specific time for inclusion before going ahead with its own merger, and, although no one could foresee the delays incident to the final approval of the I.C.C.'s plan of reorganization, such delays are not unprecedented, and it should have been clear to everyone that the assets of the Debtor could not go on absorbing the staggering operational losses over an indefinite period of months and years. The I.C.C.'s inclusion and payment order should not have caused a great deal of surprise and it does no damage to the Penn Central. Certainly neither the Commission nor the courts nor the parties ever contemplated that because no precise time was fixed for inclusion and no exact price was determined when the takeover of the New Haven became a condition of the Penn Central merger, that a long attenuated struggle over the price issue could turn inclusion into a practical impossibility.

No substantive rights of the Penn Central are lost or prejudiced by the Commission's order for immediate inclusion and payment. The principal of the amount paid on January 1, 1969, in accordance with the Commission's order, will be deposited in the registry of the court, subject to further order of the court, except that any income on said sum shall be collected by and used by the Trustees of the New Haven Railroad for the purposes of said Railroad or a successor corporation to be formed under the plan. Penn Central will be fully protected and afforded a full and fair opportunity to challenge the I.C.C.'s determination of price; and at the same time other parties in interest will have a full and fair opportunity to attack the price as too small. In the absence of an agreement by the parties to settle their differences, this case will not end with this court's present decision. In any event, whether a judgment as to the ultimate price were entered before the end of the year or several weeks hence, appeals will be taken to the Court of Appeals and the Supreme Court. No final resolution of the case can be achieved for many, many months — a time long past the power of the New Haven to survive. There has been no delay on the part of anyone; all parties have proceeded with despatch and there is nowhere a suggestion of dilatory tactics.

The order of the I.C.C. relating to inclusion of the Debtor's railroad operations in Penn Central Company on or before January 1, 1969 by conveyance of the Debtor's assets to Penn Central Company and payment of consideration therefor by Penn Central Company, as specified in the Plan, subject to the jurisdiction reserved by this court, is affirmed and the parties are directed to implement said inclusion and payment in compliance with the I.C.C.'s order. Settle order.

Dated at New Haven, Connecticut, this 24th day of December, A.D. 1968.

ROBERT P. ANDERSON
United States Circuit Judge,
sitting by designation.

Order No. 559

IN THE

UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF CONNECTICUT

In Proceedings for the Reorganization of a Railroad

In the Matter of THE NEW YORK, NEW HAVEN AND HARTFORD RAILROAD COMPANY, Debtor.	No. 30226

ORDER DIRECTING INCLUSION OF DEBTOR IN PENN CENTRAL COMPANY

The Interstate Commerce Commission (the Commission) having certified to this Court, on December 2, 1968, a Plan of Reorganization for the Debtor (the Plan), as embodied in its reports and orders of November 16, 1967 and March 1, 1968 which have been modified in accordance with its report and order of November 25, 1968, together with exhibits and a transcript of the proceedings before the Commission; this Court having, by Order of December 3, 1968, directed the filing of objections and claims for equitable treatment on or before December 16, 1968, and scheduled hearings on the Plan commencing December 20, 1968; notice of said Order of December 3, 1968 and of the hearings thereon having been duly given in accordance with said Order; all parties in interest having been given due opportunity to file their objections in writing to said Plan and their claims

for equitable treatment; the Court having, at the hearing on December 20, 1968, limited said hearing to the issue of the inclusion of the Debtor's railroad operations in Penn Central Company on or before January 1, 1969 by conveyance of the Debtor's assets to Penn Central Company and payment of consideration therefor by Penn Central Company, as specified in the Plan, subject to the jurisdiction reserved in this Order; all parties in interest having been heard or given opportunity to be heard on said issue; and this Court having filed its opinion in the premises,

THE COURT FINDS AS FOLLOWS:

1. Due and lawful notice to all persons and parties has been given in strict compliance with the Order of this Court of December 3, 1968 prescribing the manner of notice.

2. Subject to the jurisdiction reserved herein, the inclusion of the Debtor's operations in Penn Central Company as of December 31, 1968 in accordance with the Plan is fair and equitable, and otherwise fully complies with the requirements of Section 77 of the Bankruptcy Act, including subsections (b) and (e) thereof.

3. The Debtor is insolvent within the meaning of Section 77(e) of the Bankruptcy Act, and the equity of the holders of the Debtor's preferred and common stock and certificates of beneficial interest has no value.

4. Inclusion of the Debtor's operations in Penn Central Company as of December 31, 1968 by conveyance of the Debtor's assets and payment of the consideration specified in the Plan, subject to the jurisdiction reserved herein, will not adversely and materially affect any class of stockholders or of creditors of the Debtor's estate, except that under Section 77(e) of the Bankruptcy Act, the interest of the United States of America is deemed to be affected.

5. The United States of America has consented to the order of the Interstate Commerce Commission insofar as it relates to the conveyance of the Debtor's assets to Penn Central Company,

to the payment of the consideration therefor by Penn Central Company, and to the inclusion of the Debtor's railroad operations in Penn Central Company.

6. The inclusion of the Debtor's operations in Penn Central Company as of December 31, 1968 as provided herein need not be submitted for voting to any class of creditors, including the United States of America, or to the holders of the Debtor's preferred and common stock and certificates of beneficial interest.

7. The Commission has directed Penn Central Company to include the Debtor's operations on or before January 1, 1969 and to pay the consideration set forth in the reports and orders of the Commission referred to herein on December 31, 1968, regardless of then pending petitions for reconsideration or matters in litigation.

8. The foregoing findings shall be taken and deemed to be findings of fact, and in addition, to the extent appropriate, conclusions of law.

It is ORDERED, ADJUDGED AND DECREED that the order of the Commission relating to inclusion of the Debtor's railroad operations in Penn Central Company on or before January 1, 1969 by conveyance of the Debtor's assets to Penn Central Company and payment of consideration therefor by Penn Central Company, as specified in the Plan, subject to the jurisdiction reserved in this Order, is affirmed and the parties are directed to implement said inclusion and payment in compliance with the Commission's order as follows:

A. The Trustees of the property of the Debtor (the New Haven Trustees) are directed to convey the assets of the Debtor to Penn Central Company as provided in the Plan and to take any and all steps necessary and proper to effect the inclusion of the Debtor in Penn Central Company effective at 11:59 p.m. on December 31, 1968.

B. Penn Central Company is directed to include the Debtor effective at 11:59 p.m. on December 31, 1968 and to pay to the

New Haven Trustees, and the New Haven Trustees are authorized to receive, on the closing date provided in the Plan, to wit, December 31, 1968, the following consideration:

(1) 950,000 shares of Penn Central Company stock (plus such additional shares as may be necessary by the anti-dilution provisions approved by the Commission);

(2) $33,600,000 principal amount of Penn Central Company bonds;

(3) $8,000,000 in cash (less any amount representing accrued vacation pay which the New Haven Trustees and Penn Central Company agree is to be assumed by Penn Central Company); and

Penn Central Company is further directed on December 31, 1968 to assume obligation and liability in respect of:

(a) the Debtor's equipment obligations;

(b) the Debtor's Harlem River Division mortgage and bonds;

(c) the mortgage, bonds and certificates of contingent beneficial interest when issued pursuant to the Plan of Reorganization of the Boston and Providence Railroad Corporation (B&P);

(d) the payment for publicly held shares of the Boston and Providence Railroad Corporation upon consummation of the Plan of Reorganization of the B&P; and

(e) such other obligations and liabilities of the Debtor or of the New Haven Trustees, all as are provided in the reports and orders of the Commission referred to herein; and

Penn Central Company is further directed, on December 31, 1968, to cancel and surrender to the New Haven Trustees all Certificates of the New Haven Trustees held by said Company to evidence loans to the New Haven Trustees.

C. The New Haven Trustees and Penn Central Company are hereby authorized and directed to perform all obligations to be performed by them pursuant to the provisions of the Plan relating to the inclusion of the Debtor and of the operations of the B&P in Penn Central Company, including the making of adjustments on May 31, 1969, the post-closing adjustment date under the Plan, in such amounts as may be payable by the New Haven Trustees and Penn Central Company, respectively, on said date pursuant to Section 7 of the Agreement between the New Haven Trustees and the Pennsylvania Railroad Company and the New York Central Railroad Company, dated April 21, 1966, as amended (the Purchase Agreement).

D. The New Haven Trustees are authorized and directed to turn over to Penn Central Company on December 31, 1968 the operations of the B&P and all rights of the Debtor with respect to such operations, and Penn Central Company is directed to operate the B&P, subject to the reserved jurisdictions of the Commission and of this Court, pending consummation of the Plan of Reorganization of the B&P, the payment by Penn Central Company for the publicly held shares of the B&P, the conveyance of the assets of the B&P to Penn Central Company and the assumption by Penn Central Company of the obligations under the mortgage bonds and certificates of contingent beneficial interest to be issued pursuant to the Plan of Reorganization of the B&P, Penn Central Company to succeed to the rights of the New Haven upon consummation of said Plan.

E. The Clerk of this Court is directed forthwith to turn over to the New Haven Trustees for delivery to Penn Central Company on the closing date the following assets held in the registry of this Court:

(1) 5% Note of Railway Express Agency, Incorporated, in the principal amount of $1,272,284.02;

(2) $1,068,000 principal amount of The Providence Terminal Company 4½% First Mortgage Bonds;

(3) 9,551 shares of stock of Providence and Worcester Railroad Company;

(4) 1,071 shares of stock of Norwich and Worcester Railroad Company;

(5) 3,364 shares of stock of Fruit Growers Express Company;

(6) 15,000 shares of stock of The New York Connecting Rail Road Company;

(7) 7 shares of stock of The Boston Terminal Corporation; and

(8) 15,000 shares of stock of New England Transportation Company and 6% demand note of said Company in the principal amount of $738,000.

F. The Trustees under the indentures of the Debtor's First and Refunding Mortgage and of the Debtor's General Income Mortgage are hereby directed to turn over and release forthwith to the New Haven Trustees for delivery to Penn Central Company on the closing date all securities held in pledge pursuant to said indentures including the following:

(1) 25,877 shares of stock of The Pullman Company;

(2) 400 shares of stock of South Manchester Railroad Company; and

(3) Voting trust certificate substituted for 91,344 shares of stock of Railway Express Agency, Incorporated, pursuant to Order No. 510 herein.

G. All persons, firms and corporations whatsoever, and wheresoever situated, located or domiciled are directed to turn over forthwith to the New Haven Trustees for delivery to Penn Central Company on the closing date any and all of the Debtor's assets held by them, in pledge or otherwise, which are to be conveyed to Penn Central Company pursuant to the Plan.

H. The conveyance of the Debtor's assets to Penn Central Company pursuant to the Plan shall be a binding transfer to

Penn Central Company free and clear of all liens, charges and encumbrances thereon except as specified in Section 3.2 of the Purchase Agreement as modified with regard to the Harlem River Division mortgage and bonds and approved in the Plan; the liens, charges and encumbrances to which the Debtor's assets are subject prior to the conveyance of such assets shall attach and be recognized as continuing liens, charges and encumbrances upon the assets hereafter held by the New Haven Trustees, including all assets on deposit in the registry of this Court, all as provided in the Plan.

I. Upon inclusion of the Debtor in Penn Central Company, the New Haven Trustees shall be relieved of the duty to operate and manage the railroad and common carrier properties of the Debtor, including those railroad and common carrier properties operated by the Trustees under lease or other arrangement; and in all other respects, the Trustees shall have all of the authority hitherto granted them in these proceedings.

J. The conveyance of the Debtor's assets by the New Haven Trustees and the payment of consideration by Penn Central Company, as provided herein, shall be without prejudice to the right of any party to contest the fairness and adequacy of the consideration and the other terms of the inclusion of the Debtor's operation in Penn Central Company.

K. The Court hereby reserves jurisdiction to adjudicate all operations and claims for equitable treatment heretofore filed herein except that all objections to the inclusion of the Debtor's operations in Penn Central Company as of December 31, 1968 are hereby overruled and denied.

L. Upon receipt of the consideration to be paid from Penn Central Company, the Trustees shall forthwith deposit in the registry of this Court the stock and bonds of Penn Central Company received by them, pending further order of this Court upon notice to all parties, provided, however, that, until further order of the Court, the New Haven Trustees shall be entitled to receive directly payments of interest and dividends on said securities.

M. The Clerk of this Court is hereby directed to transmit a certified copy of this Decree and of the Opinion of the Court hereon dated December 24th, 1968 to the Interstate Commerce Commission.

ENTER:

ROBERT P. ANDERSON
United States Circuit Judge,
sitting by designation.

Dated: December 24th, 1968.

UNITED STATES DISTRICT COURT
DISTRICT OF CONNECTICUT

In Proceedings for the Reorganization of a Railroad

In the Matter of
THE NEW YORK, NEW HAVEN AND HARTFORD RAILROAD COMPANY,
Debtor.

No. 30226

MEMORANDUM OF DECISION ON THE ISSUE OF THE PRICE TO BE PAID FOR THE DEBTOR'S ASSETS

In 1968 both this, the Reorganization Court, and a statutory Three Judge District Court in the Southern District of New York reviewed the Second and Third (primarily the Second) Supplemental Reports of the Interstate Commerce Commission, 331 I.C.C. 643, 754, this court pursuant to §77(e) of the Bankruptcy Act, 11 U.S.C. §205(e), and the Three Judge Court pursuant to 28 U.S.C. §§1336(a), 2321-2325 applying §5(2)(b & d) of the Interstate Commerce Act (49 U.S.C. §5(2) (b & d)). By its decision of May 6, 1968[1] the Three Judge Court remanded the case to the I.C.C. for the correction of certain errors and for the recondsideration of the amount to be paid by Penn Central for the assets of the New Haven.

On August 13, 1968 the Reorganization Court filed its decision of August 13th,[2] which likewise remanded the case to the I.C.C. for substantially the same reasons. This court, however, held that because of the desperate financial condition of the New Haven Railroad, its rate of operational losses, outflow of cash, and the steady irreversible erosion of its estate, a continuance of railroad operations beyond December 31, 1968 would constitute such a taking of the New Haven Railroad's property without just compensation that it would be constitu-

tionally impermissible. It further made clear that unless the transfer of the assets of the New Haven and the operation of the transportation system were taken over by the Penn Central by January 1, 1969, the trains of the New Haven would stop running.

The I.C.C. on remand held further hearings on the issues presented and, on November 25, 1968 (service date December 2, 1968), issued its Fourth Supplemental Report and Order, 334 I.C.C. 25. This not only covered its redetermination of the price to be paid by the Penn Central for the assets of the New Haven, but also the plan for the reorganized New Haven Railroad (hereinafter referred to as "Step Two"), including the method and means of distribution to various classes of creditors. The I.C.C. certified the whole plan to this court; after due notice, certain of the parties in interest filed objections and briefs; and a hearing was held before this court on December 20, 1968 limited to that part of the Fourth Supplemental Report and Order which was crucial to the life of the New Haven.

This was the requirement that Penn Central take over the New Haven by January 1, 1969; that New Haven make a binding transfer, free and clear of all liens, to Penn Central of its assets that were to be transferred under the agreement, as amended, between Pennsylvania, New York Central and the Trustees of the New Haven; and that Penn Central concurrently pay to the Trustees of the New Haven the consideration which the Commission in its Report found to be fair and equitable.

On December 24, 1968 this court by its Order No. 559 and accompanying Memorandum of Decision approved and ordered the foregoing, without prejudice to the right of any party to contest the fairness and adequacy of the consideration.

Penn Central sought a stay of the inclusion portion of the order, both in the Three Judge Court and this court, but its petitions were denied and the transfer and payment of consideration took place as directed on December 31, 1968 — seven and one-half years after New Haven went into reorganization.

Subsequently, the fairness and adequacy of the consideration and the "Step Two" provisions of the plan came on for hearing and argument on March 31, April 1 and 2, 1969.

This opinion deals solely with the consideration, as fixed by the Commission, in its Fourth Supplemental Report and Order of November 25, 1968, *supra*.

In that Report and Order the Commission found the liquidation value of the assets to be transferred by the New Haven to Penn Central was, as of December 31, 1966, $162.7 million. It then deducted $22.1 million to make allowance for two factors; one, a reduction of $15,386,000 in the value of the estate for a 1-year delay before the start of liquidation could commence, which the Commission said would be necessary before it would issue an abandonment certificate; and, two, a bulk sale discount of $6,695,000. These items will be discussed presently, but first something should be said about liquidation value as the basis for determining price.

From the time the Trustees filed their plan with the Commission on October 27, 1966, the parties, the Commission and the courts have used the term liquidation value as an economic term to describe the best price that the existing market could fairly be expected to provide for the sale of the assets of the New Haven Railroad over a reasonable period of time, fixed by the Commission at six years. It was expected that from this gross amount the economic costs and expenses incident thereto would be subtracted to arrive at a fair liquidation value. These were such items as expenses of holding and maintaining the property during the six year period, taxes, counsel fees, costs of sale, brokerage commissions, appraisal fees, other similar expenses, and discounts for delay in receipt of proceeds; and a discount of $8 million for contingencies such as failure to sell some items and for other risks which could result from a disposal of all the assets in the six year period. No one of the parties through the inclusion hearings, nor the Commission in its Report of November 16, 1967, 331 I.C.C. 643, took the position that circumstances attending hypothetical liquidation

proceedings, such as delays in commencing those proceedings that would be occasioned by a petition for and termination of the §77 Reorganization, the subsequent accounting, setting up a liquidating equity receivership, and hearing on foreclosure of the mortgages, as well as time consumed in abandonment proceedings before the I.C.C., were factors to be considered in determining fair liquidation value. In its inclusion report the Commission spoke of the evidence received as having been "directed largely toward showing asset values upon an *assumed liquidation.*" (Emphasis supplied.) 331 I.C.C. 643, 657.

The assumption included a situation where the Railroad's operations had been lawfully abandoned and its properties were being dismantled and sold piecemeal. The Commission considered this as purely hypothetical and unlikely to occur, but in its inclusion Report of 1967, 331 I.C.C. 643, 704, it had in mind that actual liquidation would involve lengthy legal proceedings which could well burden the creditors with further operating losses. On the same page it said, "We have found herein the fair liquidation value of the NH properties and that the consideration to be paid by Penn-Central is worth at least that value", but it made no effort to reduce the fair liquidation value by any such means as it employed in its Fourth Supplemental Report of 1968. In the circumstances of this case, the proper method for determining fair liquidation value was that utilized by the Commission in 1967, although it incorrectly applied the method in some respects.

The Commission in its inclusion report gave recognition to §77(b)(5) which proscribes sales of a debtor's property for less than "a fair upset price." It found that the liquidation value of New Haven's property exceeded the fair upset price. It did not attempt to distinguish between the two measures of value or separately to define them. This court in its opinion of August 13, 1968 (289 F. Supp. at 455), discussed the history of the term, and concluded that under the circumstances of the present case and as applied to it, fair upset value means the same thing as "fair market" or "liquidation value." But

in its Fourth Supplemental Report the Commission found the liquidation value to be $162.7 million, then ordered the sale of the debtor's property for $22.1 million less. This court concludes that the Commission's order in thus reducing the predetermined liquidation value, illegally contravened the statute.

Both reviewing courts decided that under the circumstances of this case the only feasible standard for determining price must, because of both the "fair and equitable" clauses of the statutes and the constitutional mandate, be the fair liquidation value, which is the property's highest and best use. On the remand the Three Judge Court (289 F. Supp. at 441), concurred in by this court (289 F. Supp. at 454), directed the Commission as follows:

> "The Comission is therefore directed to make detailed findings as to each element of liquidation value and of the consideration to be paid by Penn Central on a basis consistent with this opinion. If it agrees with our view that the price cannot be less than the liquidation value, it shall prescribe suitable terms. If it does not, it shall state the pricing theory it has adopted, the reasons for it, and the results, and shall make whatever detailed subsidiary findings are required to support this." [Footnote omitted.]

The Commission's Fourth Supplemental Report and its counsel's express admission in oral argument before this court have made clear that the Commission neither developed nor applied a new or different pricing theory; but purported to base its determination on fair liquidation value. Its newly conceived deductions for delay in issuing an abandonment certificate and for a bulk sale discount are described by the Commission as "refinements" of the fair liquidation value theory. It also disputed the courts' interpretation of the constitutional mandate and adopted one of its own. This appears to be that the use of the pricing theory based upon fair liquidation value wholly derives from, and is completely subject to, the issuance of an abandonment certificate by the Commission, which it will not issue to a debtor, as a matter of

right, though the debtor has for many years been submerged in a deficit operation with no prospect of improvement;[5] but may grant as a privilege in its sole discretion, to be given or withheld on the conclusory basis that its action is "fair and equitable" or "required by the public interest", and apparently unsupported by anything more substantial than the Commission's own introspections or the latest word from the Cumean Sybil.

The Commission also asserts that, because the Constitution does not specify any particular method of valuation, it possesses unrestricted flexibility and range of discretion; and "due process" and "just compensation" referred to in the Fifth Amendment mean compensation based upon the value of the assets remaining after the debtor's estate has been invaded to the unlimited extent the Commission finds is called for by the paramount public interest, provided the Commission takes pains to declare it fair and equitable. This is tantamount to no constitutional protection whatever.

In this court's opinion of August 13, 1968, (289 F. Supp. at 455), it described the extent to which the bondholders' constitutional rights could be invaded in the case of a railroad in bankruptcy as follows:

> "Both the Commission and the courts, however, have reiterated in this and in related proceedings that as bondholders of a railroad their interests are subject to such invasion as may be essential to continue the operation of the railroad for a reasonable period of time to provide an opportunity to work out a permanent plan or means of continuing the operation, if possible, to the extent that it is required by the public interest." [Footnote omitted.]

The Three Judge Court described the extra burden imposed upon the creditors of a railroad at this stage of a reorganization as follows:

> "Although we agree that by investing in a railroad the bondholders did not surrender their constitutional right not to be required to operate the property at a perpeutal loss,

they did subject themselves to such interim losses as are reasonably incident to working out the solution most consistent with the public interest." 289 F. Supp. 418, at 444.

By late 1963 it was clear to the Trustees of the New Haven and to the Reorganization Court that only two courses were open: the Trustees must press to accomplish the inclusion in a Penn Central merger or they must press for liquidation. The former was obviously in the public interest and the latter was not. The course of inclusion was followed; but because the merger and the reorganization proceedings stretched out far beyond what was originally forecast, the "interim" became seven and a half years; and "losses reasonably incident to working out the solution most consistent with the public interest" eroded the debtor's estate in excess of $60 million.[6]

In addition to increasing the burden of these losses, the Commission asserts the power to hold up liquidation of a railroad, long operating deeply in the red, not only for a reasonable time to provide an opportunity to work out a permanent plan or means of continuing operations, but for as long a period or periods as the Commission finds there is "a hope of a public takeover of segments" to provide states and communities an opportunity to present their plans.

Like Laban of old, the Commission would now require further servitude of the debtor — in this case the creditors. But the duty of the debtor's creditors to suffer losses for an interim period has already been fulfilled and the public interest has already been served to the extent that in fairness and equity the public had any right to demand. This proposition is clear beyond doubt. The public interest may well have been over protected. There was certainly no under protection. The solution most consistent with the public interest has been worked out and the I.C.C. has no power or right to require more.

Putting to one side, momentarily, the constitutional bar to the imposition of further losses on the New Haven, something should be said regarding the gross unfairness and inequity of imposing such losses in the name of the public interest. During

seven and one-half years, the Federal government, the states, the communities and the public in general were fully informed by the Trustees of the Railroad as to the inability of the New Haven to survive as an independent railroad. And, apart from seeking inclusion in a merged Penn Central, the Trustees were engaging in a holding operation to afford the public bodies, as the real guardians of the public interest, the opportunity to act — to take over or adopt measures to preserve the New Haven transportation system. Response to this was partial tax assistance and, in the latter half of the period, grants which covered about ⅓ of the annual passenger losses. New York and Connecticut, acting through Tri-State Transportation Commission and with Federal aid, contemplate contracting for the purchase of railroad passenger transportation for the west-end commuter service in and out of New York — a project which is still going forward and is now being worked out with the Penn Central. Similarly, a contract was made by the Massachusetts Bay Transportation Authority for commuter service in the greater Boston area. Otherwise nothing has come to the attention of this court, to indicate anything more than a highly speculative prospect, that any or all of the states concerned or their municipalties had the slightest interest in taking over and operating the New Haven or any segment of it.

In spite of full awareness of the situation of the bankrupt line and with nothing to prevent their doing so, no standby legislation, for use if inclusion of the New Haven by Penn Central fell through, was ever enacted or sought to be passed in seven and one-half years by the Federal Government or by any of the states for the take over and operation of the New Haven freight and passenger system or a segment of it (except for the west-end and the Boston commuter services); nor was any plan ever filed by the governmental bodies incorporating such take over and operation. If inclusion by the Penn Central had not been achieved and no such standby legislation had been passed, the cost of the failure of the governmental bodies to act must, according to the Commission, be chargeable to the New Haven estate to afford the governmental bodies an additional

opportunity to decide whether they wish to take steps to keep all or a part of the railroad in operation. Assuming, as the Commission has, that there is no constitutional bar, such a second round of loss superimposed on the first, like Pelion on Ossa, is as unfair and inequitable as can be imagined, nor does the Commission suggest any limitation on itself. Apparently once it has decided that operation of even a segment is in the highest public interest, it may require a third and fourth round of losses to the estate so long as it can envision over the horizon a new hope that some person or group may take over and operate such a segment of the New Haven.

It is also inequitable to penalize the New Haven an additional $15,386,000 as the consequence of delaying abandonment in a hypothetical liquidation proceeding, so that the political units and representatives of the public interest could be heard, when, but for the adoption by the Trustees of a course to serve the public interest, abandonment proceedings could and would have been commenced in late 1963 and liquidation would have been started, certainly by the valuation date of December 31, 1966.

The policy of imposing an interim burden of losses, through its deficit operation, on a railroad in reorganization is to afford a reasonable opportunity to the responsible agencies to arrange the continuation of the railroad's operation, but the law does not require the furnishing of two or three or four opportunities. The duty was more than amply fulfilled by the New Haven. The public interest has had one huge bite of the apple; it is not entitled to another.

This court adheres to the position that due process and just compensation provisions of the Fifth Amendment prohibit the imposition of a further period of erosion of assets on the New Haven. It has ruled that any erosion additional to that accumulated through 1968 would be constitutionally impermissible as a taking without just compensation. But in its Fourth Supplemental Report the Commission asserts that the constitutional limitation sets up no standard of value and is very

flexible, so that it leaves the Commission with an almost completely unrestricted discretion so long as it declares that its decision is fair and equitable and in the public interest. The Three Judge Court and this court rejected that legal principle in their former opinions, 289 F. Supp. 418 at 440-441 and 289 F. Supp 451 at 459; and the law as established by these courts was the law of the case which the Commission should have followed.

The Commission had argued that the constitutional right of a deficit operated railroad to cease operation and liquidate, as recognized by Supreme Court cases, had been considerably modified by later statutes.

Judge Friendly, in writing for the Three Judge Court, fully answered this as follows at p. 441:

> "We cannot accept the argument that all this was changed by the addition of §1(18), requiring the Commission's consent to abandonment, to the Interstate Commerce Act by the Transportation Act, 1920, or by the enactment of §77 of the Bankruptcy Act in 1933. These statutes were designed to assure orderly procedures and to afford methods that might avoid the ultimate solution; they were not intended to override constitutional guarantees, cf. In re Third Avenue Transit Corp., 198 F.2d 703, 707 (2 Cir. 1952), and would not be effective if they had been." [Footnote omitted.]

Now the I.C.C. argues that the leading case in support of the courts' position, *Brooks-Scanlon Co.* vs. *Railroad Commission of Louisiana*, 251 U.S. 396 (1920), and the subsequent cases relying on it, were overruled, sub silentio, by *Colorado* vs. *United States*, 271 U.S. 153, 156, 168 (1926), in which, the Commission says, its "role in weighing the advantages and disadvantages of an abandonment of branch lines that lose money was preserved . . . The Supreme Court in our view has never flatly held that a deficit-ridden railroad has an absolute right to abandon, liquidate and sell the parcels." 334 I.C.C. at pp. 55-56.

As this interpretation of the applicable law is the key to the Commission's conception of the scope of its own power, which in turn underlies most of the extraordinary and unprecedented actions taken by the Commission in formulating its Fourth Supplemental Report and Order as they affect the matter of price, it is necessary to go into an analysis and discussion of the pertinent cases.

The factual setting, for the legal principles to be expounded, is unique. New Haven's deficits were not limited to unprofitable segments of an overall profitable system. Quite the contrary. New Haven's long-time deficits were system wide. And it is this court's conclusion from an examination of the cases, that the I.C.C. is plainly in error in the legal principles which it advanced.

Brooks-Scanlon Co. vs. *Railroad Commission of Louisiana, supra,* held unconstitutional the State Commission's attempt to compel a lumber company, whose overall operations were profitable, to continue the operation of a railroad which, after the exhaustion of the timber which it had originally been constructed to haul to the company's sawmills, had no profits and no prospect of any. The Court unanimously held that the State's action deprived the company of its property in violation of the Fourteenth Amendment. Justice Holmes' opinion said, *inter alia,* "A carrier cannot be compelled to carry on even a branch of business at a loss, much less the whole business of carriage . . . ." 251 U.S. at 396. He cited *Munn* vs. *Illinois,* 94 U.S. 113 (1876), apparently merely for its dictum that one who devotes his property to public use and thereby subjects it to regulation "may withdraw his grant by discontinuing the use." 94 U.S. at 126.

The holding of *Brooks-Scanlon* was reaffirmed in *Railroad Commission* vs. *Eastern Texas R. Co.,* 264 U.S. 79 (1924). In that case the railroad, another intrastate line originally constructed to serve logging industries, operated at a deficit after the timber ran out. Nevertheless, it continued to operate until it had exhausted both cash and credit. (Unlike *Brooks-Scanlon* and like the New Haven, the line was not part of a generally profitable business enterprise.) The State attempted

to enjoin abandonment (which the I.C.C. had authorized) and dismantling. Again a unanimous Supreme Court, citing *Brooks-Scanlon,* held that, in the absence of contract, a carrier could not constitutionally be compelled to operate at a loss. The Court said (264 U.S. at 85):

> "The company, although devoting its property to the use of the public, does not do so irrevocably or absolutely, but on condition that the public shall supply sufficient traffic on a reasonable rate basis to yield a fair return. And if at any time it develops with reasonable certainty that future operation must be at a loss, the company may discontinue operation and get what it can out of the property by dismantling the road. To compel it to go on at a loss *or give up its salvage value* would be to take its property without the just compensation which is a part of due process of law" (emphasis supplied).

The Court conceded, as it had in *Brooks-Scanlon,* that if a railroad did desire to continue its operations, the State might compel it to provide adequate service to the public, even though compliance might be "attended by some pecuniary disadvantage." *Ibid.*

Where and in what way these cases were overruled sub silentio by *Colorado* vs. *United States,* 271 U.S. 153 (1926), must be apparent only to the wishful thinking of the Commission for nothing in the holding or dicta of that case conveys any such suggestion to a reader who is trying to find it. There the I.C.C. had authorized an interstate railroad, whose operations were generally profitable, to abandon an unprofitable intrastate branch, finding that its continued operation at a deficit would impose an undue burden on interstate commerce. The State brought suit to enjoin compliance with the order. The sole issue was the respective areas of state and federal jurisdiction, specifically whether Congress could constitutionally give a federal agency power to authorize the abandonment of an intrastate branch, and the Court's holding was simply that, since the operation of the branch had an effect on the road's interstate operations,

"the exercise of federal power in authorizing abandonment is not an invasion of a field reserved to the State." 271 U.S. at 161. No issue of constitutional right to abondon was presented. The State assumed the validity of *Brooks-Scanlon* and *Eastern Texas;* indeed, it relied on their dicta to support its argument that the railroad had no right to abandon a losing part of the line while continuing to enjoy the privilege of operating profitable parts within the State. The Court cited *Eastern Texas* with apparent approval. The I.C.C.'s version of the decision is probably based on a dictum that Congress had made public necessity and convenience the sole test of authority to abandon. 271 U.S. at 168. But the statement was not made in the context of a discussion of a constitutional right to abandon, and it seems in the last degree unlikely that Justice Brandeis, who wrote the opinion, intended to make a gratuitous asertion, overruling prior decisions of the Court, that a carrier could be compelled to operate at a loss for however long a time public convenience and necessity might require such operation. Ten years after the decision of the *Colorado* case the Court cited both *Brooks-Scanlon* and *Eastern Texas* for the precise proposition that "a common carrier cannot be compelled to carry on business indefinitely at a loss."[7] *Pacific Telephone & Telegraph Co.* vs. *Tax Commission*, 297 U.S. 403, 413 (1936). See also *Mora* vs. *Mejias*, 223 F.2d 814, 818 (1 Cir. 1955). Actually Justice Brandeis' dicta in *Pacific Telephone* went further: "If, because of such loss, a corporation, seeing no prospect of betterment, wished to discontinue its local business and were prevented by law from doing so unless it discontinued also its interstate business, the law might be held void as imposing an unconstitutional condition upon the privilege of engaging in interstate commerce." 297 U.S. at 413.

It should be noted that the question of the I.C.C.'s power to compel a carrier to operate in the financial circumstances of *Brooks-Scanlon* and *Eastern Texas* (which were essentially the same as the New Haven's, which all concerned, including the Commission, agreed had no prospect of profitable operations) has never been litigated. In the somewhat similar case of the

New York, Ontario and Western, the Commission did in fact authorize abandonment. See 334 I.C.C. at 59. But there is no reason to suppose that the limitation which the Fifth Amendment places on federal power to compel carriers to operate at a loss is any weaker than the restriction which the Fourteenth Amendment places upon the power of the States to do so. *Cf. In re Third Avenue Transit Corp.*, 198 F.2d 703, 707 (2 Cir. 1952).

The Commission also suggested that *Brooks-Scanlon* and *Eastern Texas* somehow rested on the method of determining value for rate-making purposes which was prescribed by *Smyth* vs. *Ames*, 169 U.S. 466 (1898); and that their basis was destroyed when the case was overruled by *Federal Power Commission* vs. *Hope Natural Gas Co.*, 320 U.S. 591 (1944), which held that the F.P.C. might use any method of valuation in fixing a rate, so long as the result was "just and reasonable". The Commission attached much weight to the Court's statements that "there are no constitutional requirements more exacting than the standards of the [Federal Power] Act" and that a "rate order which conforms to the latter does not run afoul of the former." 334 I.C.C. at 57. But these statements do not, of course, suggest that Congress could provide a criterion for rate making which did not meet the Fifth Amendment's standard of "due process." The Act required the Federal Power Commission to set rates which were "just and reasonable", and the Court's assumption that a "just and reasonable" rate of return on investment is due process seems unquestionable. It may be arguable, as the I.C.C. suggested, that a deficit-ridden railroad has no absolute right to abandon, but only a right to stop the deficits (334 I.C.C. at 56), but the distinction is academic here where it would be impossible to set a rate which would yield a "just and reasonable" or "fair and equitable" return (or any return at all) upon investment. *Brooks-Scanlon* and *Eastern Texas* did not in any way depend upon the particular method employed to reach the conclusion that the operations of the

carriers could not yield a fair return on investment. The *Hope* case is irrelevant to the issue in the present case with which the Commission was dealing.

This court, therefore, concludes that *Brooks-Scanlon* and subsequent cases, reaffirming the validity of its holding, are still applicable and determinative. The Commission is unable through a groundless construction of statutes, as noted above, to eliminate the constitutional guarantees applicable to this case. And it may not arrogate to itself a vast expansion of power through a strained interpretation of Supreme Court decisions.

There remains its claim that the use of the term "fair liquidation value" demands the consideration of and deduction from gross liquidation proceeds of all the burdens, delays, costs and expenditures derived from court and Commission proceedings to terminate a reorganization effort and institute an equity receivership to effect a liquidation. While in the present case the Commission referred only to the delay attendant upon leave to abandon, it is equally logical to hypothesize all of the steps which would necessarily precede actual liquidation. The Commission never entertained any such concept on the first round. If there is only one exclusive and universally recognized meaning to the term fair liquidation value and that meaning must include all steps in liquidation proceedings, it is indeed strange that the I.C.C. did not consider it in the Second and Third Supplemental Reports. Its declared reasons for not doing so are transparent pretexts under the cover of which the Commission arbitrarily and capriciously confers a benefit — not on the public — but on Penn Central, which would obtain New Haven's assets at a price substantially below fair liquidation value and yet comply with the condition for the Pennsylvania-New York Central merger that it take over the New Haven.

As previously stated, the term "fair liquidation value" has been used in the present case to describe a method or theory of determining value. It envisioned sales of New Haven property over a period of six years and of economic factors related

to the business process of turning the properties into cash. It was a method of getting at fair market value less the costs and expenses incidental to the selling program.

The hypothesis did not include an analysis and computation of costs, expenditures and delays in terminating the reorganization proceedings, commencing an equity receivership, and seeking abandonment and liquidation. It was limited to determining price through the historically recognized theory of fair liquidation value in a context where all elements of a sale were present and only price remained to be fixed. There was nothing in the actual facts of the case which required a hypothetical concept which included a consideration of all the legal proceedings from termination of the reorganization to completion of liquidation. Neither the hypothetical concept nor the actual case requires consideration of such legal proceedings. It was not until the Fourth Supplemental Report that the Commission hauled in by the heels the issue of the right to abandon as a condition precedent to liquidation, and used it as an arbitrary device to reduce what it found the liquidation value to be, i.e. $162.7 million, because it felt that figure was too high to be fair and equitable to Penn Central. But in the very Report and Order in which it fixed that liquidation value it ordered inclusion and payment to be made by January 1, 1969, thereby, in effect, not only approving but directing abandonment of the New Haven and liquidation of its assets.

Turning now to the additional deduction (referred to as the bulk sales discount) of $6,695,000 subtracted by the Commission from liquidation value, it is the conclusion of the Reorganization Court that this deduction is also improper and without support in law or reason. It is predicated on the fact that Penn Central is purchasing all of the New Haven's assets at one time. The Commission explains it as giving recognition to the price differential between sales at wholesale and retail. There is nothing in the record to show that such a thing as a wholesale market for all of New Haven's railroad properties exists. There is apparently no retail market either.

Value, under the circumstances of this case, can only be arrived at through the dismantling of the transportation plant and a piece by piece sale of the properties. It is clear from the record that a market existed for the disposition of the properties on this basis. Their value is the best price the market place will give the seller, less the costs and expenses relevant to the sale, as more fully mentioned above. It makes no difference whether the purchaser wants to use the property as is, or to improve and develop it. The question is how much will the market place give for a particular item of property. This must be arrived at through the testimony of experienced and qualified experts, as was done in this case. The Commission and Penn Central urge that Penn Central should be credited with a bulk sales discount for removing from the debtor's estate the risk of non-sale or of sale below fair market value. But the computation in arriving at fair liquidation value has already deducted $8,000,000 for this purpose, in addition to costs and expenses attending the sale of the properties. It is true that a bulk purchase would eliminate all of these expenses and the risks of marketing the properties over a span of 6 years, but in arriving at fair liquidation value, which is a net value, all of these items were deducted. Now the I.C.C. would give Penn Central an encore — the gift of a double deduction.

Further the bulk sale deduction violates the fair upset value minimum for sales of a debtor's property, as provided in §77(b)(5), because "fair upset value" is the lowest price the debtor's estate could accept for the properties. That lowest price is what the market would pay, which is implicit in the standard used here, i.e. fair liquidation value. Neither a trustee nor an equity receiver could, with the court's approval, sell for less.

The Commission appears to place some reliance in its brief on quoted portions of this court's opinion of August 13, 1968 to support the Commission's view that the fairness standard is the ultimate test of a constitutional price for the New Haven. This reliance is misplaced. Contrary to the Commission's statement that the Reorganization Court disavowed any fixed mini-

mum price that the Constitution might require, this court fully concurred with the Three-Judge Court's conclusion that fair liquidation value was a mandatory constitutional minimum. On page 459 of that opinion this court said, ". . . the constitutional minimum of value of property rights to which the bondholders are entitled (in this case the liquidation value as of December 31, 1966) . . ." made clear what the court had in mind.

Grand Central Terminal Properties

The bondholders attack the Commission's valuation of New Haven's interest in the Grand Central properties on several grounds. With all except one, this court neither finds that plain error was committed by the I.C.C. nor that its conclusions were unfair or inequitable. The claim that there is value to the New Haven's right of access to the Grand Central Terminal requires some comment in view of this court's suggestion in its August 13, 1968 opinion that the Commission consider and make findings as to what value, if any, attached to what the court considered a valuable interest. After reading the briefs and hearing the arguments of all those who urged this point, and those opposed, the court is now satisfied that the Commission's treatment of the matter must stand. The Special Master and the Three Judge Court concluded there was no value in the interest, principally because it is not the kind of interest that would survive liquidation; nor, if it did, could it be assigned. Moreover, there was no evidence that the expenses of maintaining the terminal would be any less. And the idea that the State of New York, or an interstate authority might pay, directly or indirectly, some consideration for availing itself of that use is highly speculative in view of the bargaining positions of the states and the disposition of the I.C.C. to require Penn Central to furnish such access free of charge to a state or public authority which assumed the commuter service, as a condition of Penn Central's getting rid of that much of the losing and burdensome passenger service. While mitigation of a burden may in some circumstances furnish a consideration, it is not a measurable one for the purpose of this issue in the case.

The one claim made by the bondholders which points to plain error on the Commission's part relates to New Haven's claim to accrued excess income for the years 1967 and 1968. This is not a matter of valuation at all, but is an accounting matter for income received, to which the New Haven is entitled to one-half. Penn Central argues, and the Commission held, that because the value of the hotel properties was computed, on the basis of capitalization of earnings, as of December 31, 1966, all income thereafter was covered by that computation and to permit the New Haven to share in the income thereafter, would afford it a double allowance. This is manifestly wrong. Current earnings and expenditures, relating to the properties assumed to be liquidated, continued until the transfer of the assets to the Penn Central. If Penn Central were permitted to retain this excess income for 1967-68, it could, on the same principle, claim all the rents collected by the New Haven on all its leased property and all of the freight and passenger revenues. Correlatively, fairness and equitability would require that Penn Central pay all of the losses for the same period. New Haven's 50% share of the excess income for 1967 and 1968 should be paid over or credited to it by Penn Central at the post-closing adjustment at the end of May, 1969.

Harlem River & Oak Point Freight Yards

In considering the claims of the parties relating to the Harlem River and Oak Point Freight Yards in connection with the inclusion report or the first round of hearings, this court decided that the I.C.C.'s acceptance of the lower of two appraisals for industrial use attributed to appraiser McCann, i.e. $18.1 million rather than $22.65 million, was supported by substantial evidence and could not be set aside as unfair or inequitable. McCann himself did not testify on the first round and, therefore, there was no cross-examination to probe the basis for his conclusions. His appraisals came in through witness Thompson, head of the New Haven's real estate department. From this it appeared that McCann's higher figure was based flatly on the assumption that the properties were fully operating railroad

yards. His lower figure was based upon the assumption that, coincidental with the liquidation of the New Haven, all of the tracks would have been pulled up and removed and the properties would be left without electricity or any power — in short, non-railroad served real estate. On this state of the evidence there seemed to this court no reason to disturb the Commission's finding.

At the hearings on the second round McCann did testify. He revealed that at the time of the appraisal made for Thompson and put into the record through the latter's testimony, he, McCann, was entirely unaware that the Port Morris branch of the Penn Central bordered or came to the edge of the Oak Point Yard. A rail connection was presumably available through a spur track connection. Actually, the lines on the property on December 31, 1966 connected with the Port Morris branch line and there was nothing to require the tearing up and removal of the tracks from the property upon liquidation of the New Haven. Nor was there any showing of a necessity to do so. Penn Central, in effect, argues that it would refuse to make an agreement for a spur track connection because of the large expense of removing certain clearance problems on its own branch (a point which was largely refuted by some of its own evidence) as well as difficulties with car classification, and because the revenues from indusrial users of these yards would not warrant it. The Commission accepted this argument and made its decision on that basis. The conclusions required to be reached for such a decision were not, however, supported by substantial evidence and cannot stand. It is undisputed that the Port Morris branch was and is there and operating and Penn Central has not been authorized to abandon it. Instead of assuming that the industrial development of the 160 acres of the two yards would not make a spur track connection economically feasible, the Commission should have concluded precisely the opposite.

The tracks running through these yards are the connecting link between both the Penn Central's Port Morris branch and

the Hunts Point Wholesale Market erected by the City of New York at a publicly announced cost of approximately $100 million dollars, and between that market and the New York Connecting Railroad. The great bulk of produce for feeding of the millions of residents of metropolitan New York is brought in by rail through these yards to this market and distribution point. To assume that the State and City of New York would stand idly by and permit the life line to its huge and costly enterprise to be cut, just as it is in the midst of planning its necessary enlargement, because it was unwilling or unable effectively to bring pressures to bear or take steps on its own to preserve the connection with Penn Central is absurd, even if the I.C.C. continues its policy of forcing the railroads to handle perishable produce at a loss. Under circumstances where the City of New York may itself have acquired the line running through the yards, it is certainly unlikely that Penn Central could then deny a spur track connection to industrial owners and users of the property in question. In fact, it is probable that the business from the industries would tend to reduce the losses incurred, if any, in serving Hunts Point. It is far from clear why the Commission concluded that Penn Central would be compelled to give the State of New York, or its transportation authority, free access to the Grand Central Terminal for passenger trains operated by the State because of its economic strength, political pressures, and the requirements of the public interest, and in the next breath took the view that the City or State, or both, could not acquire a connection with Penn Central for its Hunts Point Market which is equally important to the City of New York and the public interest. As a matter of law the Commission should have adopted McCann's appraisal of these yards with rail service at $22.7 million rather than his appraisal without rail service at $18.1 million, which requires an addition to fair liquidation value of $4.6 million.

Failure of I.C.C. to correct understatement of liquidation value by deducting $16.2 million in accrued real estate taxes.

Both this and the Three Judge Court directed the Commission to remove from its calculations of liquidation value the sum of $16.2 million of accrued real estate taxes on property to be transferred free and clear of liens. In the Fourth Supplemental Report it complied to the extent of $14.6 million, and left $1.6 million as a part of the liquidation expenses.

The Commission's reason for this bizarre result is that the reorganization plan itself calls for the payment of these accrued taxes in notes payable over a period of time. It found that the market will discount the notes by 10% or $1.6 million from their face value and, therefore, this amount should, in effect, be subtracted or remain subtracted from the fair liquidation value. But this does not follow. The Commission was directed to remove the tax obligation from all consideration of fair liquidation value because it has nothing to do with that subject, and all $16.2 million must be so removed. The $16.2 million of accrued taxes remains an obligation of the estate. How the tax, bond and other creditors deal with it has nothing whatever to do with fair liquidation value, and is of no concern to Penn Central, as purchaser.

Valuation of the 950,116 shares of Penn Central stock

In arriving at a valuation of the 950,116 shares of Penn Central stock transferred by Penn Central as part of the purchase price for the assets of the New Haven Railroad, the Commission, presumably in an effort to assure fairness to Penn Central, did not use the market value of December 31, 1966 or an average of the values at or about December 31, 1968, the actual date of transfer. Instead, it adopted the theory that, after all, the purpose of using stock in payment was to tap the expected future economic benefit of the Penn Central merger which would come to full fruition seven to ten years after its effective date on February 1, 1968, but would be reflected in an upward trend of the stock at the time of closing or transfer of New Haven's

assets to Penn Central, then estimated to be in 1970. The expert testimony in January 1967 forecast that the stock would fluctuate between $75 and $100 per share at the closing, about three years thereafter. The Commission found this a fair basis for valuation corroborated by its own calculations based on the 1965 income of the Pennsylvania and New York Central Railroads, adjusted by estimated merger savings. This mean of the range of prices per share of Penn Central, estimated for the time of closing, was $87.50 and this was adopted as the stock's value.

Although contested by the bondholders, both courts accepted this per share value in their 1968 opinions on the inclusion report, the bondholders renewed their attack on the second round, and the matter was again heard by the Commission, which adhered to its original decision. Again objections have been pressed in both courts. The bondholders assert that fairness and equity require that the value should have been based on the market value of December 31, 1966 — the valuation date for everything else — or on the average market for a reasonable period of time before the date of closing. The average market price on December 30, 1966 (the last trading date of 1966) was 52⅜. The closing price on December 31, 1968 was 63⅜. The average of the high and low prices for November and December 1968 was 62.81. The bondholders claim it is unfair to charge the New Haven's estate with having received $83.1 million when the form in which it was received could be acquired on the open market for about $20,000,000 less.

Nevertheless, the theory of giving recognition to an intrinsic value in the shares, which will be realized when the full economic benefits of the merger have been achieved, not only assists the Penn Central by relieving it of the need to divest itself of a crippling amount of cash, which would be prejudicial to its merger program, but affords the New Haven an opportunity to participate in probable future profits.

There is an element of unfairness, however, in the fact that the New Haven has transferred assets conservatively worth what the liquidation value says they are worth. The purchase price,

to the extent of $83.1 million and fully credited to the purchaser as $83.1 million paid, is not worth $83.1 on the present market. It is credited as $83.1 paid, on an assurance or asumption that the 950,116 shares will be worth that sum and more, but when and who will make good on that assurance is not known or not stated. The ordinary purchaser of shares of stock takes it subject to his losing or gaining on the money he put into it. But the New Haven is not that kind of a purchaser; it is being compelled to take it at a substantial present loss on an assurance of future gain. But suppose the shares never go to 87½ in the whole ten years to February 1, 1978?

The nub of the unfairness and inequity is not the 87½ fixed for present calculations, but the fact that the purchaser is getting assets of sure present value while the seller is asked to gamble for its payment on the future of the Penn Central.

This consideration does not require a change in price or an amendment to the valuations tabulated by the Commission. To be fair and equitable, however, it does require a supplemental provision fulfilling the implicit promise by the purchaser to pay $83.1 million as part of the price for the assets conveyed. This may readily be done by the Reorganization Court and does not call for a remand. Therefore, the order is amended to provide in addition that if at any time the market price of Penn Central common shares reaches and maintains 87½ per share on the New York Stock Exchange for a period of five consecutive days on which the Exchange is open and doing business (not counting days on which the Exchange is closed to trading) between the date of final consummation of the plan of reorganization and February 1, 1978, then and in that event it will be conclusively presumed that Penn Central has, in transferring the shares to the New Haven, made payment of the $83.1 million of the purchase price represented by the shares. If, however, the common shares of Penn Central do not reach and maintain the price as aforesaid, then the value of the shares will be determined by the average of the means between high and low prices of Penn Central shares on the New York Stock Exchange for the

30 business days next preceding February 1, 1978, on which the Exchange is actually operating and there are sales of Penn Central shares. Penn Central will forthwith become liable to pay in cash to the New Haven, or its successor or successors, the difference between said mean market prices of those 30 days and 87½ for each share of the block of 950,116 shares.

The benefit of this underwriting by Penn Central of any difference between the mean market prices of the shares for those 30 days and the higher price of 87½ per share and the right to recover that difference, inure only to the New Haven and its successor or successors, and do not follow the shares into the hands of a purchaser if they are sold. The right to recover the difference is, however, not lost to the New Haven even if it sells all or a portion of the 950,116 shares, provided, of course, that the circumstances described as giving rise to the right, occur. The Penn Central is granted an option, operative between the date of final consummation of the plan and February 1, 1978, to discharge its obligation to underwrite and pay the difference between such average market price and the higher 87½ at the end of the ten year period by paying on one or more blocks of 50,000 shares to the New Haven or its successor or successors, the difference between the mean market prices for sales of Penn Central common shares and 87½ per share as of a specific day of sales on the Exchange which shall previously have been designated by Penn Central in a written notice delivered to the New Haven at least 5 days prior to such market date.

These provisions to assure full payment of $87.50 per share are not to be construed by the New Haven or its successor or successors as a directive or limitation on its handling of the Penn Central shares which it owns, either to sell or retain them in whole or in part, and it is intended to leave those responsible for the affairs of the New Haven with the same freedom to exercise their sound judgment in the company's interest, subject to law, as they would have had in the absence of such provisions.

Valuation of Boston and Providence CCBIs.

The Commission was in error in placing a value of $1.5 million on the CCBIs issued by Boston and Providence Railroad Corporation which inured to the New Haven and which were acquired by Penn Central. There is no competent evidence to support such a valuation and the whole concept of requiring Penn Central to pay for them is wrong. The CCBIs represent an obligation to pay out to former shareholders of Boston & Providence 52% of the net proceeds from the sale of real estate, which Penn Central has purchased, when, as and if that real estate or portions of it are sold under certain windfall conditions. In effect, the Commission's action would cause Penn Central to pay something for the privilege of later paying itself the 48% of such net proceeds if the contingencies occurred with respect to property Penn Central had already bought and paid for.

Discount on proceeds from liquidation of New Haven's assets.

In the inclusion report the Commission found that the proceeds from the liquidation sale would be $197.9 million and discounted it for present value by $17.6 million. In the Fourth Supplemental Report it made three valuation changes: (1) it added $2.6 million for increased value of the New Haven's interest in the Boston & Providence, (2) subtracted $6.2 million for its reductions in property values, and (3) subtracted $3 million for 1966 depreciation. It did not, however, change the amount of discount but left it at the old, inapplicable figure of $17.6 million.

The Commission will, therefore, on or before June 11, 1969 file with the Reorganization Court, with copies to all parties of record, a new formulation and computation of the discount for present value of the New Haven's liquidation proceeds, in accordance with generally recognized accounting principles and based upon the changes made in valuation items through and including those stated in the present opinion. This may be in the form of a letter or short brief. Other parties in interest will, on or before June 18, 1969 file with the court their com-

ments thereon and any formulations and computations of their own, in accordance with such accounting principles, in a letter or brief.

Cost to Penn Central

It is unnecessary for the Reorganization Court to discuss in detail the Commission's findings and conclusions regarding the cost to Penn Central of the inclusion of the New Haven. One item of cost listed by the Commission is, however, wholly untenable and that is the $14.0 million attributed to Penn Central's burden of early inclusion. Because actual inclusion took place on December 31, 1968 instead of in November of 1970, as the Second and Third Reports and Orders contemplated, the Commission created a kind of right in Penn Central not to be required to take over the New Haven until 1970. But there never was any such right. The Pennsylvania and New York Central Railroads did not have to purchase their right to merge at the price of including the New Haven if it found the price too great. But they accepted these terms and merged on February 1, 1968. The Penn Central's duty to include the New Haven arose at that time, though no specific date was fixed for performance. While the agreement between the railroads and the Trustees of the New Haven assumed it would be at the time of final confirmation of the reorganization plan, that agreement never became binding in all its provisions. The purpose of the inclusion was to continue most of the railroad services furnished by the New Haven. It was abundantly clear by the end of January 1968 that the New Haven would not be able to continue its operations into 1970. Penn Central was under an obligation to take over the transportation plant of the New Haven whenever it could be tendered free and clear of liens and the I.C.C. and the courts ordered it to do so. Under the pressure of economic necessity the orders issued and inclusion actually took place on December 31, 1968; but this imposed no additional duty on Penn Central, above and beyond the obligations it had already agreed to assume.

With regard to other issues raised or objections made, including those which concern purchase price adjustments under §9 of the agreement between the Trustees of the New Haven and the Pennsylvania and New York Central Railroads, there is not sufficient substance or merit to them to warrant interference with the Commission's Fourth Supplemental Report and Order.

Subject to any further hearing which may hereafter be found to be necessary, this court is now of the opinion that there should be only one order issued for Steps One and Two, implicit in the Fourth Supplemental Report and Order certified to this court and now being reviewed, and that order will await the court's opinion on Step Two of the Reorganization Plan; therefore, no order will be issued at the present time except for a special order relating to the single issue of the 1967 and 1968 excess income from the Grand Central properties. As mentioned earlier, this is not a part of the purchase price but is a simple matter of accounting for income received by Penn Central and not paid over. One-half of this excess income, which is readily ascertainable, is due from Penn Central to the Trustee for the New Haven and is ordered to be set off against any sum this court may order the Trustee of the New Haven to pay Penn Central as a partial settlement in the course of approving the petition for order No. 572.

Dated at New Haven, Connecticut, this 28th day of May, A.D. 1969.

ROBERT P. ANDERSON
United States Circuit Judge,
sitting by designation.

FOOTNOTES:

[1] 289 F. Supp. 418.

[2] 289 F. Supp. 451.

[3] The Commission makes reference to this court's opinion of August 13, 1968 as support for the correctness of its deduction from fair liquidation value for losses pending abandonment proceedings. This court said, 289 F. Supp. at 459, "While liquidation will have to await authority to abandon, the trains will stop in January because . . . actual operation of the Railroad will cease." This was, however, in the event that the Commission did *not* order inclusion by January 1, 1969. Even if this had happened, it was not contemplated by this court that abandonment proceedings would take more than four to six weeks. The New Haven had been studied, examined and reported on almost continuously since 1957. For the seven and a half years of the reorganization the states, municipalities and the federal government had been heard over and over again. Nothing more than pro forma abandonment proceedings were called for. It is of interest to note that the application for abandonment in the case of the Tennessee Central Railway Company, Finance Docket #24964, 333 I.C.C. 443, was filed February 12, 1968 and the certificate and order permitting abandonment was issued April 25, 1968.

[4] At the end of the discussion of fair upset price this court noted there was some authority that it may be less than "fair market" or "liquidation" value at least where the purchaser is a public authority, according to a 1911 decision of a federal court in New Hampshire, cited in the margin. It was referred to as a matter of historic interest and not as in any way applicable to the present case, which concerns purchase by a private corporation. In view of the Commission's assertions of power in its Fourth Supplemental Report to order a sale, in the name of the public interest, to a purchaser who agrees to operate the railroad, for a price less than the fair liquidation or fair salvage value, it becomes necessary for this court to note its disagreement with the Commission's claim and with the 1911 New Hampshire case to the extent it may lend support to the Commission in this regard, because of the constitutional infirmity of the position in authorizing a sale for something less than just compensation.

[5] Inclusion Report of I.C.C., dated November 16, 1967, 331 I.C.C. at 687: "If there is one thing on this record that is clear and undeniable, it is that NH has neither earning power nor the prospect of earning power."

331 I.C.C. at 697: "The cold, hard fact is that NH has been losing money for years and that unfortunate situation continues unarrested."

[6] See 334 I.C.C. at 126, Appendix 4, Classification of Claims: A, B, D, E, F, totalling $63,868,000.

[7] It now appears that the Commission's notion that *Colorado* overruled *Brooks-Scanlon, sub silento,* was only a temporary aberration. In Tennessee Central Railway Co., abandonment of operations Docket #24964, 333 I.C.C. 443, decided April 25, 1968, the Commission said at 452, "It is well established that a carrier should not be required to continue in the business of carriage when its overall operations are conducted at a system-wide deficit for a substantial period of time and where there is no reasonable prospect of the applicant's conducting those operations at a profit for the foreseeable future. Compare *Brooks-Scanlon Co.* vs. *Louisiana R. Comm.*, 251 U.S. 396 (1920), and *Chicago N. S. & M. Ry. Abandonment of Entire Operation,* 317 I.C.C. 191 and 363."

Order No. 572

IN THE

UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF CONNECTICUT

In Proceedings for the Reorganization of a Railroad

In the Matter of THE NEW YORK, NEW HAVEN AND HARTFORD RAILROAD COMPANY, Debtor.	No. 30226

ORDER APPROVING A PARTIAL SETTLEMENT WITH PENN CENTRAL COMPANY, SUBJECT TO AN OFFSET, AND FOR WITHDRAWAL FROM REGISTRY OF THE COURT OF A CERTAIN AMOUNT OF FUNDS TO AID IN MAKING THE PARTIAL SETTLEMENT

The Court having filed on May 28, 1969 its Memorandum of Decision on the Issue of the Price to be Paid for the Debtor's Assets and having found therein that the Trustee is entitled to one-half of the excess income from the Grand Central Terminal Properties for 1967 and 1968 and that this amount should be offset against the amount due Penn Central Company under the Section 7 settlement referred to in said petition;

The petition of the Trustee of the property of the Debtor for approval of both a partial and, subsequently, a final settlement with Penn Central Company and for withdrawal from the registry of the Court of a certain amount of funds to aid in making said settlements, and so much of said petition that deals with a partial settlement having come on for hearing, which was duly noticed pursuant to the order of this Court, and

all parties in interest having been heard or given opportunity to be heard; and

The Court being duly advised in the premises;

It is ORDERED that:

1. The Trustee is entitled to one-half of the excess income from the Grand Central Terminal Properties for 1967 and 1968.

2. The Trustee is entitled to a partial offset of $2,000,000 of the aforesaid amount against the partial settlement of $6,872,729.58 set forth in said petition, with a final offset to be made at the final settlement. The aforesaid partial offset is without prejudice to the rights of both the Trustee and Penn Central Company as to the amount of the final offset.

3. The partial settlement as set forth in said petition is hereby approved, subject to the aforesaid partial offset, and the Trustee is authorized to pay to Penn Central Company on May 29, 1969, the amount of $4,872,729.58; and the payment by the Trustee and receipt by the Penn Central Company of said amount are without prejudice to the rights and liabilities of the Trustee or Penn Central Company as determined by the arbitrator for the Section 7 settlement referred to in said petition.

4. The Trustee is authorized to withdraw from the registry of the Court 60%, or approximately that percentage, of the $4,872,729.58 to be paid, to aid in effecting the partial settlement that is hereby approved.

5. The Trustee is authorized to take such other steps as are necessary and appropriate for the accomplishment of the foregoing.

ENTER:

ROBERT P. ANDERSON
United States Circuit Judge,
sitting by designation.

Dated: May 28, 1969.

Supplemental Order No. 572

IN THE

UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF CONNECTICUT

In Proceedings for the Reorganization of a Railroad

In the Matter of
THE NEW YORK, NEW HAVEN AND HARTFORD RAILROAD COMPANY,
Debtor.

No. 30226

SUPPLEMENTAL FINDINGS AND ORDER FIXING TERMS OF FINAL SETTLEMENT BETWEEN TRUSTEE AND PENN CENTRAL COMPANY UNDER SECTION 7 OF AGREEMENT DATED APRIL 21, 1966, AS AMENDED

The Court having entered on May 28, 1969 its Order No. 572 approving a partial settlement by the Trustee of the property of the Debtor with Penn Central Company pursuant to Section 7 of the agreement between the New Haven Trustees and The Pennsylvania Railroad Company and The New York Central Railroad Company, dated April 21, 1966, as amended (the "Purchase Agreement"), subject to an offset; and having ordered therein that the Trustee of the property of the Debtor is entitled to one-half of the excess income from the Grand Central Terminal properties for 1967 and 1968; and having provided that a final offset would be made at the final settlement of said Section 7; and

Notice having been given on May 29, 1969 that the further hearing on final settlement would be held June 24, 1969, with a closing to be held at the office of the Trustee on June 25, 1969; and

The matter having come on for hearing on June 24, 1969 pursuant to said notice, and all parties in interest having been heard or given opportunity to be heard;

The Court being duly advised in the premises, hereby finds as follows:

1. The total amount to be paid by the Trustee to Penn Central pursuant to Section 7 of the Purchase Agreement is $7,712,681.27, of which $4,872,729.58 has heretofore been paid on May 29, 1969 pursuant to Order No. 572;

2. The Trustee is obligated to Penn Central in the amount of $99,011.22, heretofore received and held by the Trustee, representing payments on Recollectible Costs in the total amount of $349,207.74 required to be carried by the Trustee as of December 31, 1968 in the Debtor's Account No. 743, and will be further obligated to Penn Central on any additional amounts hereafter so collected on said $349,207.74;

3. Penn Central is obligated to the Trustee in the amount of $275,000 on account of a payment in such amount made by the Trustees to the United States pursuant to Order No. 565;

4. Penn Central is obligated to the Trustee in the amount of $45,000 heretofore received and held by Penn Central representing payments of condemnation awards related to takings prior to December 31, 1969 of property of the New Haven;

5. Penn Central is obligated to the Trustee in the amount of $3,377,903.07 on account of the one-half share of excess income of Grand Central Terminal properties for 1967 and 1968 to which the New Haven is entitled; and

6. The final settlement herein under Section 7 should net the other amounts owed and that, accordingly, the amount to be paid by the Trustee to Penn Central under finding 1 should be increased by the amount set forth in finding 2 and offset by the amounts owed by Penn Central to the Trustee as set forth in findings 3, 4 and 5; and, therefore,

It is hereby ORDERED, ADJUDGED AND DECREED that:

A. Penn Central pay $758,940.16 to the Trustee of the Debtor;

B. The Trustee of the Debtor pay to Penn Central all amounts collected after June 23, 1969 on the $349,207.74 of Recollectible Costs included in the Debtor's Account No. 743 at December 31, 1968; and

The Clerk of this Court is hereby directed to transmit a certified copy of these Supplemental Findings and Order to the Interstate Commerce Commission.

ENTER:

ROBERT P. ANDERSON
United States Circuit Judge,
sitting by designation.

Dated: July 1, 1969.

Penn Central is granted a stay in paying the aforesaid $758,940.16 for 10 days, and, if an appeal is taken by it during that time, then during the pendency of the appeal.

ROBERT P. ANDERSON
United States Circuit Judge,
sitting by designation.

Dated: July 1, 1969.

UNITED STATES DISTRICT COURT

DISTRICT OF CONNECTICUT

In Proceedings for the Reorganization of a Railroad

In the Matter of THE NEW YORK, NEW HAVEN AND HARTFORD RAILROAD COMPANY, Debtor.	No. 30226

MEMORANDUM OF DECISION ON DISTRIBUTIVE OR STEP II PORTION OF FOURTH SUPPLEMENTAL REPORT AND ORDER OF INTERSTATE COMMERCE COMMISSION

Following the Fourth Supplemental Report and Order of the Interstate Commerce Commission, 334 I.C.C. 25, dated November 25, 1968 and the Commission's certification of a Plan of Reorganization to this court on December 2, 1968, this court on December 24, 1968, by its Order No. 559 and its accompanying Memorandum of Decision, approved and ordered the transfer of substantially all of the assets of the Debtor railroad (New Haven) to the Pennsylvania Central Company (Penn Central), free and clear of all liens. The transfer was to be effected by January 1, 1969; Penn Central was concurrently to pay to the Trustees of the New Haven the consideration which the Commission in its Report found to be fair and equitable; and all of this was to be without prejudice to the right of any party to contest the fairness and adequacy of the consideration. The foregoing was accomplished on December 31, 1968.

Subsequently, after notice to all parties in interest, this court held a hearing on March 31 - April 2, 1969 on the issue of price and the distributive or Step II provisions of the Plan; and on May 28, 1969 filed its Memorandum of Decision on the Issue of Price.

The court then believed, or at least hoped, that in a short time it would be feasible for it to pass definitively on all remaining issues, i.e., the distributive provisions of the Plan of Reorganization, as certified to this court by the I.C.C.; and that a remand of the Plan to the Commission might not be necessary. It was encouraged in this belief by the constructive opinion of the Commission's counsel that a remand to the Commission would not be required to overcome the objections of the administration claimants in Class A and Class B. These classes deal, respectively, with counsel fees, and with the trustees' certificates. Their treatment is hereinafter discussed. A more troublesome problem concerns the settlement and payment in cash of claims, up to the time of the consummation of the Plan, where that would be mutually beneficial to the claimant and to the estate. It is not unlikely that this problem could also have been resolved without a remand to the Commission, or by a very restricted remand limited to that matter.

A subsequent event of major impact, however, has altered this promising outlook and it now appears that it is necessary to remand the Plan and that it be held by the Commission in abeyance until the matter of price is determined with finality. The Three Judge Court in the Southern District of New York rendered its opinion on June 18, 1969, one judge dissenting in part, concerning the same issue of price dealt with by this Reorganization Court on May 28th; but that court approached the most important issues in a substantially different manner and reached a widely different result. The additional price to be paid by Penn Central, as fixed by this Reorganization Court, is approximately $29 million more than the Commission by its Fourth Supplemental Report ordered Penn Central to pay. The Three Judge Court's majority opinion, however, approved in substance the Commission's order, although it directed the Com-

mission to serve a proposed decree, which "among other things, shall reflect in dollar amounts the changes directed in this opinion". Pursuant thereto the Commission by its Fifth Supplemental Report and Order of July 10, 1969, service date July 11, 1969, 334 I.C.C. 528, purported to increase by $5.33 million the consideration to be paid by Penn Central. But erroneously included in this ostensible price increase is $3.38 million, which represents a debt due by Penn Central to New Haven for the latter's one-half interest in the excess income of the Grand Central Terminal properties for 1967 and 1968, and is not a part of the price to be paid by Penn Central for New Haven's assets. Since the Three Judge Court has not yet acted upon the Commission's Fifth Supplemental Report, it is not known whether it agrees with the position of this, the Reorganization Court, although its opinion reads as if it were in accord. Be that as it may, the increase in price ordered by the Commission's Fifth Supplemental Report is only $1.95 million; and, therefore, the present price differential between the Reorganization Court and the Commission is approximately $27 million.

This price difference alone makes appeals and cross-appeals from both courts inevitable. If this conclusion needs buttressing, it is supported by at least three additional factors:

(1) The payment by Penn Central and receipt of the consideration by New Haven on December 31, 1968, as heretofore mentioned, was without prejudice to the right of any party (including Penn Central) to contest the fairness and adequacy of the consideration.

(2) The ultimate value of New Haven's interest in the Grand Central Terminal properties might far exceed that which this court has found. Take, for example, only one item, although a major one, and that is the value of New Haven's right of access to the Grand Central Terminal, which the I.C.C. found to be of no value—a determination which this court finally concluded in its Memorandum of May 28, 1969, could not be disturbed, although in its opinion of August 13, 1968 (289 F. Supp. 451, at 463), it was of the view that on remand the I.C.C. should recon-

sider on the basis that the New Haven's right was valuable. If on appeal the existence of such a right were to be recognized, the evidence presently in the record would show a potential worth of approximately $70 million.

(3) The price of $87.50 attached by the Commission and this court to the Penn Central stock for purposes of partially satisfying Penn Central's obligation to New Haven raises a serious issue, even though this court provided a formula for payment in its Memorandum of May 28, 1969, which has since been adopted in substance by the I.C.C. in its Fifth Supplemental Report.

The ultimate matter of price is far too much at large for the Reorganization Court presently to determine whether the Plan of Reorganization "affords due recognition to the rights of each class of creditors", §77(e), which includes not only the bondholders but also one other pre-reorganization class of claimants—claims of state and local authorities for pre-reorganization secured tax claims (Class H)—and six classes (Class A through Class F, inclusive)[1] of administration claimants. Further, if this court were now so venturesome as to approve the Plan in substance, how could the various classes of creditors vote intelligently on it? It is abundantly clear in the present posture of the case that approval must await a final determination as to price and, presumably, that issue can be definitely determined only by the Supreme Court, unless a settlement between the parties in litigation can be effected and approved by this court and other authorities, if necessary.

• • •

[The remainder of the opinion deals with "Step II" issues and has been omitted in printing.]

Dated, July 28, 1969

ROBERT P. ANDERSON,
United States Circuit Judge,
sitting by designation

IN THE

UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF CONNECTICUT

In Proceedings for the Reorganization of a Railroad

In the Matter of
THE NEW YORK, NEW HAVEN AND HARTFORD RAILROAD COMPANY,
Debtor.

No. 30226

ORDER ADJUDGING THE PRICE TO BE PAID BY PENN CENTRAL COMPANY; APPROVING AND DISAPPROVING CERTAIN STEP II PROVISIONS OF THE PLAN; AND REMANDING TO THE COMMISSION

By order entered August 12, 1968, this court disapproved the First Step of the Plan of Reorganization of the Debtor certified to it on March 29, 1968 by the Interstate Commerce Commission (the "Commission") and referred the proceedings back to the Commission for further action. Thereafter, on December 2, 1968, pursuant to §77(d) of the Bankruptcy Act, the Commission certified to this court a Plan of Reorganization for the Debtor (the "Plan") as set forth in the Commission's Fourth Supplemental Report on Reconsideration and Further Hearing, dated November 25, 1968 (334 I.C.C. 25). By Order of December 3, 1968, this court directed that any objections to the Plan and claims for equitable treatment be filed on or before December 16,

1968. On December 20, 1968, this court held a hearing on the Plan limited, however, solely to the issue of inclusion of the Debtor's railroad operations in Penn Central Company (the "Penn Central") in view of circumstances then existing. This court then entered Order No. 559, dated December 24, 1968, directing that the Trustees of the property of the Debtor (the "Trustees") convey the Debtor's assets to Penn Central and effect the inclusion of the Debtor in Penn Central, effective at 11:59 p.m. on December 31, 1968, and that Penn Central then carry out such inclusion and pay to the Trustees certain specified consideration, assume certain obligations and liabilities and cancel and surrender specified Trustees' Certificates, all as provided in the Plan. On January 29, 1969, the Trustees reported as to compliance with Order No. 559, and this court entered Order No. 563, dated February 27, 1969, approving the report.

Subsequently, after notice to all parties in interest, this court held a hearing on March 31, April 1 and April 2, 1969 on the issue of price and the distributive or Step II provisions of the Plan; and on May 28, 1969 filed its Memorandum of Decision On the Issue of the Price to be Paid for the Debtor's Assets (the "Memorandum On Price"). And, in connection therewith, having found that Penn Central is indebted to the Debtor for 50% of the so-called excess income from the Grand Central properties for 1967 and 1968, and that this is not a part of the price to be paid by Penn Central for the Debtor's assets, this court entered its Order No. 572, dated May 28, 1969, adjudging that the sole remaining Trustee of the Debtor is entitled to a partial offset of $2,000,000 of the aforesaid amount against the partial settlement, then approved, between the Trustee and Penn Central pursuant to Section 7 of the Agreement dated April 21, 1966; and the matter having come on for final settlement this court entered its Supplemental Order No. 572, dated July 1, 1969, adjudging that Penn Central was indebted to the Trustee in the amount of $3,377,903.07 on account of the aforesaid excess income for 1967 and 1968, approving the final settlement pursuant to Section 7 of the aforesaid Agreement, and adjudging that Penn Central pay the balance due of $758,940.16 to the Trustee of the Debtor.

I.

On June 9, 1969, this court entered its order to settle decree in accordance with the Memorandum On Price and the matter having come on for hearing and all parties in interest having been heard or been given an opportunity to be heard, this court now finds and concludes, as a matter of law, that:

1. The sums of (a) $15,386,000 as a consequence of possible delay in abandonment and (b) $6,695,000 as a bulk sales discount should not be deducted from the Commission's finding of liquidation value;

2. The value of the Harlem River and Oak Point Freight Yards is $22.539 million, which is an increase of $4.439 million over the amount found by the Commission;

3. The sum of $1.6 million should be added to liquidation value inasmuch as it was improperly deducted in respect of tax obligations;

4. The sum of $1.5 million should be deducted from the liquidation value inasmuch as it was improperly attributed to the so-called "CCBIs" to be issued by Boston and Providence Railroad Corporation;

5. The sum of $2,415,899 should be added to liquidation value inasmuch as it was improperly deducted in applying the discount to present value found by the Commission; and

6. The value of the 950,116 shares of common stock delivered by Penn Central on December 31, 1968 to the Debtor is $83.1 million, subject to the provisions hereinafter set forth in ordering Paragraph B; and

ORDERS that

A. The additional price to be paid by Penn Central to the Debtor is $29,035,899.

B. If at any time the market price of Penn Central common shares reaches and maintains 87½ per share on the New York Stock Exchange for a period of five consecutive days on which

the Exchange is open and doing business (not counting days on which the Exchange is closed to trading) between the date of final consummation of the Plan of Reorganization and February 1, 1978, then and in that event it will be conclusively presumed that Penn Central has, in transferring the shares to the New Haven, made payment of the $83.1 million of the purchase price represented by the shares. If, however, the common shares of Penn Central do not reach and maintain the price as aforesaid, then the value of the shares will be determined by the average of the means between high and low prices of Penn Central shares on the New York Stock Exchange for the 30 business days next preceding February 1, 1978, on which the Exchange is actually operating and there are sales of Penn Central shares. Penn Central will forthwith become liable to pay in cash to the New Haven, or its successor or successors, the difference between said mean market prices of those 30 days and 87½ for each share of the block of 950,116 shares.

The benefit of this underwriting by Penn Central of any difference between the mean market prices of the shares for those 30 days and the higher price of 87½ per share and the right to recover that difference, inure only to the New Haven and its successor or successors, and do not follow the shares into the hands of a purchaser if they are sold. The right to recover the difference is, however, not lost to the New Haven even if it sells all or a portion of the 950,116 shares, provided, of course, that the circumstances, described as giving rise to the right, occur. The Penn Central is granted an option, operative between the date of final consummation of the Plan and February 1, 1978, to discharge its obligation to underwrite and pay the difference between such average market price and the higher 87½ at the end of the ten year period by paying on one or more blocks of 50,000 shares to the New Haven or its successor or successors, the difference between the mean market prices for sales of Penn Central common shares and 87½ per share as of a specific day of sales on the Exchange which shall previously have been designated by Penn Central in a written notice delivered to the New Haven at least 5 days prior to such market date.

II.

On July 28, 1969 this court having filed its Memorandum of Decision on Distributive or Step II Portion of Fourth Supplemental Report and Order of Interstate Commerce Commission (the "Memorandum on Step II"), the court now finds and concludes, as a matter of law, that:

1. The additional price to be paid by Penn Central, as hereinabove adjudged by this court, is so much greater than that approved by the Three Judge Court in the Southern District of New York in its opinion on June 18, 1969, that it is not now feasible for this Reorganization Court to approve the Plan;

2. All costs and expenses referred to in Class A of Section II of the Plan should be paid in cash; and the provisions in Section V, 1. Class A should be modified accordingly;

3. The terms of the Trustees' Certificates referred to in Class B of Section II of the Plan should be observed; and the provisions of Section IV, 1, and Section V, 1. Class B should be modified accordingly;

4. The Plan should provide that any claim covered by it can be settled and liquidated in a different manner than that provided in the Plan, subject to the approval of the Reorganization Court, up to the time of the consummation of the Plan or a time prior to consummation if the Commission finds that would be more feasible and proper;

5. Unsecured pre-reorganization taxes have no equity; and the Plan properly provides that they take nothing;

6. Pre-reorganization secured tax claims and related charges of State and local authorities are entitled to interest accrued thereon prior to July 7, 1961 — the date the reorganization proceeding was instituted; but are not entitled to any post-reorgani-

zation interest. As thus construed, all of the provisions of Class H of Section V, 2, including disallowance of penalties, and that payment be made by issuance of income notes, are approved;

7. All of the provisions of Class D of Section V, 1, including disallowance of interest and penalties on post-reorganization claims of State and local authorities for taxes and related charges, and that payment be made by issuance of income notes, are approved;

8. Section V, 2, Class J of the Plan is approved insofar as it provides that the first mortgage bondholders are entitled to an accrual of interest up to but not beyond the effective date of the Plan; but insofar as it accords different treatment in the payment of principal and interest it is disapproved, and these bondholders should receive common stock for both principal and interest accrued as aforesaid;

9. Section V, 2, Class K of the Plan is modified to provide that the income bondholders are entitled to payment of their principal and interest accrued for the years 1957, 1958, and 1959; and is approved in other respects;

10. All other provisions of the Plan are approved, subject to the Commission's authority to implement the Plan and the modifications hereinabove set forth; and

ORDERS that:

A. The Plan is remanded to the Commission to be held by it until the issue of price to be paid by Penn Central is finally determined.

B. When the price is finally determined, the Commission may reconsider the Plan vis-a-vis the two system mortgages and other interested parties, to determine how the additional consideration, if any, is to be paid and whether this or a reduction in the price will require a modification in the structure of the Plan.

C. Subject to findings and conclusions 2-10, inclusive, and ordering paragraph B above, the Commission is authorized and directed to implement the Plan in any and all respects to the end that the Plan as revised will in all respects be fair, equitable and feasible.

D. This order is to be interpreted in accordance with this court's Memorandum on Step II.

ENTER:

ROBERT P. ANDERSON
United States Circuit Judge,
sitting by designation.

Dated: July 28, 1969.

Opinion of the Three-Judge Court Relating to the I.C.C.'s Second Supplemental Report

THE NEW YORK, NEW HAVEN AND HARTFORD RAILROAD COMPANY, FIRST MORTGAGE 4% BONDHOLDERS' COMMITTEE, *et al.*,

Plaintiffs,

v.

UNITED STATES of America and Interstate Commerce Commission, *et al.*,

Defendants.

United States District Court

S. D. New York.

July 10, 1968.

Before FRIENDLY, Circuit Judge, and WEINFELD and LEVET, District Judges.

FRIENDLY, Circuit Judge:

For the fourth time this Court has before it an order of the Interstate Commerce Commission in the Penn-Central merger—this one relating to the terms for the inclusion of The New York, New Haven and Hartford Railroad Company (NH).[1] The principal decision under review is a Sec-

[1] The earlier proceedings are recounted in Erie-Lackawanna R.R. v. United States, D.C., 259 F.Supp. 964 (1966), rev'd, Baltimore & O. R. Co. v. United States, 386 U.S. 372, 87 S.Ct. 1100, 18 L.Ed.2d 159 (1967); Oscar Gruss & Son v. United States, D.C., 261 F.Supp. 386 (1966), vacated and remanded for further consideration, 386 U.S. 776, 87 S.Ct. 1478, 18 L.Ed.2d 520 (1967); and Erie-Lackawanna R.R. v. United States, 279 F.Supp. 316 (1967), aff'd with minor modifications, Penn-Central Merger and N & W Inclusion Cases, 389 U.S. 486, 88 S.Ct. 602, 19 L.Ed.2d 723 (1968).

ond Supplemental Report on Further Hearing, hereafter "the Report," 331 I.C.C. 643 (1967);[2] there is also a Third Supplemental Report on Reconsideration, I.C.C. (1968). In five consolidated actions holders of various NH bonds and trustees under NH bond indentures (all collectively referred to hereafter as "the bondholders") challenge the Commission's conclusion that a Purchase Agreement between the Pennsylvania and the Central on the one hand and the Trustees of NH on the other dated April 21, 1966, and an interim loan arrangement set out in the Report constitute "just and reasonable" and "equitable" terms within §§ 5(2) (b) and (2) (d) of the Interstate Commerce Act. Erie Lackawanna R. R. has intervened, under the broad provisions of 28 U.S.C. § 2323, to assert an unrelated claim that the Commission erred in failing to set conditions to protect its interchange with NH at Maybrook, N. Y., similar to those prescribed for the benefit of the Central Railroad of New Jersey, the Reading and the Western Maryland. With some regret in view of the public urgency of effecting inclusion of NH in Penn-Central, we are constrained to vacate the order and remand for expeditious proceedings and further report by the Commission.

We begin by noting the somewhat curious posture in which, so far as concerns the bondholders' actions, the case comes to us. Since 1961 NH has been in reorganization under § 77 of the Bankruptcy Act in the District of Connecticut under the supervision of Judge Anderson. The Commission's report approved the sale of NH to Penn-Central not only under § 5 of the Interstate Commerce Act but as a means for the execution of a plan of reorganization

[2] Where page references are not otherwise identified they are to this Report.

of NH under §§ 77(b)(5) and (d). The latter determination must be certified to the District Court for Connecticut, which may approve it only if that court finds the plan "fair and equitable," § 77(e), with review of its decision lying in the Court of Appeals. When the bondholders' actions were filed, the United States moved for dismissal on the ground that the reorganization court had exclusive jurisdiction. We denied the motion in a memorandum, the salient portions of which are reproduced in the margin.[3] We adhere to the view there expressed; unfortunate as the duplicitous

[3] "The action are clearly within the letter of 28 U.S.C. §§ 1336(a) and 2321–25, and we find nothing in § 77 or in the decisions cited by the United States that would supersede this. There is, indeed, an area of overlap between the work of the two courts. We must determine, among other things, whether there is substantial evidence to support the figure fixed by the I.C.C. as the price to be paid by Penn Central for the assets of the New Haven, and the reorganization court must decide whether the plan, importantly including the price, is fair and equitable. Since the scope of the reorganization court's inquiry may well be broader than that of a court of three judges reviewing a § 5 order, we can conceive of circumstances where it would be appropriate for the latter, not indeed to dismiss as the United States urges, but rather to stay its own proceedings pending decision by the bankruptcy court. See Kansas City Southern Ry. Co. v. United States, 282 U.S. 760 [51 S.Ct. 304, 75 L.Ed. 684] (1931); Landis v. North American Co., 299 U.S. 248 [57 S.Ct. 163, 81 L.Ed. 153] (1936).

"We are convinced, however, that it would not be appropriate for us to do this, at least at this time. The complaints raise certain issues, notably the need for imposition of protective conditions pending consummation of the inclusion and the loss-sharing formula as to the loan, which may not be within the jurisdiction of the bankruptcy court. It may also be doubtful whether Penn Central would be bound to accept modifications proposed by the bankruptcy court to the same degree as in a direct review of the Commission's order, although the bankruptcy court, of course, is free, subject to normal review, to refuse inclusion of the New Haven save on terms it deems appropriate.

"We therefore think it best that proceedings should continue in the two courts."

system of review may be, we see no basis on which we can properly decline to exercise the jurisdiction conferred upon us by 28 U.S.C. §§ 1336(a) and 2321-25. Compare General Protective Committee for Holders of Option Warrants of United Corp. v. SEC, 346 U.S. 521, 74 S.Ct. 261, 98 L.Ed. 339 (1954); Phillips v. SEC, 388 F.2d 964, 969 (2 Cir. 1968).

I. *The Commission's Approach to the Valuation of NH.*

In determining fair and equitable terms for the sale of NH, the Commission was faced with a task far more difficult than the one it had just performed in setting terms for the acquisition of Erie-Lackawanna, D & H and B & M by the Norfolk & Western, see Erie-Lackawanna R.R. v. United States, supra, 279 F. Supp. at 337-340, 342-345; 389 U.S. at 523-526, 88 S.Ct. 602. Those three roads had, or were claimed to have, earning power. Here, because of the large and increasing losses of NH, the Commission properly found, 658, that "Past experience * * * furnishes no basis for valuing NH from an earnings standpoint except to emphasize the chronic deficit character of the operation which is likely to persist and render the operation a burden rather than in income producer." [4] A fair price for NH on

[4] The Commission estimated that the annual burden to Penn Central of operating NH, after taking into account economies from consolidation of some $5 million, was $8.5 million. A study made for certain of the bondholder groups—projected only until 1965 and thus not taking account of the deterioration experienced since that date—estimated that as a freight only operation NH would earn $7 million, to which the study added $5.5 million of savings from inclusion in Penn Central. However, the assumption that Penn Central would be allowed to abandon the NH's passenger service is unrealistic, and the NH trustees thought that as an independent freight-only railroad NH would no more than break even. See 658–59.

the usual basis of capitalization of earnings would thus be negative or, at best, zero; on the other hand NH is conceded to have a very substantial liquidation value.

The Commission discussed the valuation problem at several places. It began by noting, 656-58, that in the negotiations leading to the agreement between the acquiring railroads and the NH trustees "asset value was the primary determinant rather than earning power," and that the evidence before it "was directed largely toward showing asset values upon an assumed liquidation." After saying that "This approach had the appearance of satisfying" the provision in § 77(b) (5) that the means for execution of a plan of reorganization might include "the sale of all or any part of the property of the debtor either subject to or free from lien at not less than a fair upset price," it continued that "We do not look upon liquidation value as necessarily being the equivalent of 'a fair upset price'" since "liquidation contemplates a dismantling of the railroad and, therefore, an abandonment of the railroad's operations—eventualities hardly likely, in view of our findings in the prior reports herein that the services of NH are essential." It thought that "a fair upset price should be geared to the requirements that very large segments of the railroad, though probably not all, would have to be maintained in operation" through purchase by public agencies. The Report states that in such event "the pricing would be lower than a complete liquidation could produce"—without however, elucidating on what basis NH could be required to sell property to public authorities for less than liquidation value. The Commission concluded this portion of the discussion by saying that "if the consideration to be paid is the equivalent of the liquidation value, it will exceed the fair upset price contemplated by section 77(b) (5)."

After extensive discussions and findings as to the liquidation value of NH, the value to NH of the consideration under the Purchase Agreement, and the cost of the acquisition to Penn-Central, the Commission stated its summary and conclusions as follows, 697-98:

> As detailed earlier, we have found the liquidation value of NH to be $125 million. We have also found that the value to NH of the consideration to be received is $125 million. It is evident, therefore, that the consideration is at least equivalent to the liquidation value and[it] will, therefore, be equitable to all parties having an interest in the NH estate to approve the transaction.
>
> From the point of view of Penn-Central, we have found that the total cost to them of acquiring the assets is $159 million. In these circumstances, it would be unfair to Penn-Central to require them to pay a price greater than that agreed upon in the purchase agreement.
>
> Penn-Central must assume a loss-operation which not merely lacks promise of foreseeable recovery, but in fact is plagued by an unrelenting erosion. Thus, they are faced with constantly diminishing going concern values. The cold, hard fact is that NH has been losing money for years and that unfortunate situation continues unarrested. As thorough as may be the analyses forecasting profitable operations for NH as a freight-only railroad, they are subject to the fulfillment of a number of conditions and the achievement of proposals as yet untested by experience. We cannot give such projections as much weight as the actual operating results of many years.

The Commission's final words on the subject came in a portion of the opinion dealing with the Trustees' application under § 77. Here the Commission said, 724-25:

> Although earning capacity is usually looked upon as the principal criterion in valuing railroad properties, due consideration may be accorded to other relevant factors, including original cost of the properties, cost of reproduction new, cost of reproduction depreciated, actual investment therein, severance or strategic value, contributed traffic, value of particular facilities, and the effect of potential operating economies. We have given due consideration to past, present and prospective earning power as well as to other delevant factors specified in section 77 (e), including reproduction and original costs, and, additionally we have considered the liquidation value of NH—finding that value to be $125 million, a figure comparable to the price in the purchase agreement. Moreover, the liquidation value of the NH properties in the context of the NH's present situation exceeds the fair upset price, and as indicated, under section 77(b) (5) all or any part of a debtor's property may be sold at not less than a fair upset price.
>
> Those who have a valuable interest in the NH estate could not, under circumstances favorable to them in a liquidation, expect to effect a greater net return then would be accorded them under the plan we are approving herein for the sale of the assets to Penn-Central. All have had fair and ample opportunity to present evidence and argument on the question of valuation, and we find the record entirely adequate to make possible and to support findings as to that issue for all purposes of section 77 of the Bankruptcy Act as well as section

5(2) of the Interstate Commerce Act. Accordingly, the sale of NH assets to Penn-Central under the terms of our decision herein is consistent with section 77(b)(5) in that it provides an adequate means by which the trustees' plan can be executed. We also find that the consideration to be paid for the assets of NH constitutes just and adequate compensation. As we view the situation, the parties holding a present interest in NH will receive the economic equivalent of what is surrendered upon the sale of the NH assets.

The impression we derive from all this is that the Commission understandably avoided the hard decision whether a deficit ridden railroad could fairly be sold for less than its very substantial liquidation value by finding that under the Purchase Agreement liquidation value was received and thus the transaction was not unfair to NH. Since the validity of the latter inference would be indisputable, we shall first examine whether substantial evidence supported the Commission's finding of equivalence. If it did, we need go no further; if it did not, we must consider whether the Report can nevertheless be sustained.

II. *The Liquidation Value of NH.*

As indicated, the Commission made findings as to (1) the liquidation value of NH on December 31, 1966, (2) the value of the consideration payable by Penn Central, and (3) the cost of the acquisition to Penn Central. It found the first to be $128.9 million which it "rounded off" to around $125 million; the second to be $123.6 million which it again "rounded off" to around $125 million; and the third to around $159 million. In analyzing these findings,

we shall endeavor to be ever mindful of the limited scope of our review, see Erie-Lackawanna R. R. v. United States, 279 F.Supp. at 337, and cases there cited, and of Mr. Justice Cardozo's warning, "An intelligent estimate of probable future values, * * * and even indeed of present ones, is at best an approximation. There is left in every case a reasonable margin of fluctuation and uncertainty." Dayton Power & Light Co. v. Public Utility Comm'n, 292 U.S. 290, 310, 54 S.Ct. 647, 657, 78 L.Ed. 1267 (1934).

While we agree with the Government that in many instances the bondholder seek to have us substitute our judgment for the Commission's[5] and display a disturbing tendency to add apples to cucumbers by conceiving NH as operating and not operating at one and the same time, we nevertheless find the Commission's figures for liquidation value significantly too low and for value of consideration significantly too high. In this section of the opinion we shall discuss the former.

(1) *Failure to discount expenses of liquidation.*

We begin with what appears to be an obvious error by no means unsubstantial in amount. The Commission

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[5] We are totally unpersuaded by the bondholders' argument that because they claim the Commission's decision deprives them of their constitutional rights, Ohio Valley Water Co. v. Ben Avon Borough, 253 U.S. 287, 40 S.Ct. 527, 64 L.Ed. 908 (1920), requires *de novo* judicial review of the evidence rather than the substantial evidence test. The *Ben Avon* doctrine has never been applied except as to rate-making. Under the gloss of St. Joseph Stock Yards Co. v. United States, 298 U.S. 38, 56 S.Ct. 720, 80 L.Ed. 1033 (1936), it is unclear that the decision would be read today as requiring a more intensive judicial scrutiny than is generally employed in judicial review of agency decisions. See 4 Davis, Administrative Law, § 29.09 at 167 (1958).

found that liquidation of NH would require time, which it assumed to be six years. It projected the receipts over this period and discounted them to present value, applying a factor of 6%. Recognizing that so large a program would entail substantial expenses including continued accrual of property taxes, it estimated these for each of the six years—a total of $58.23 million. However, it did not discount the expenses to present value. If future receipts are to be discounted to present value, as they properly should, future expenses must likewise be. The obligation to pay $1,000,000 six years hence no more entails a present cost of $1,000,000 than a right to receive $1,000,000 six years hence is an asset in that amount.

The Report makes no attempt to explain its inconsistent treatment of the credit and debit sides of the ledger. The Commission's defense on brief is wholly unsatisfactory. It suggests that if a discount is to be applied to the liquidation expenses, a partially compensating downward adjustment should be made in the properties' assessed market value to reflect the fact that deferring tax payments by selling properties subject to tax liens depresses the sales price below the face value of the lien. The Trustees could, however, avoid this result simply by discharging the tax liens shortly before sale—under the contemplated liquidation schedule sufficient funds would be available for these and all other expenses. While it is difficult for us to determine the proper amount of the discount on the present record, it seems likely that, as the bondholders claim, this would be between $5 and $6 million.[6]

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[6] At the same time we reject an argument of the bondholders that since the Commission's estimates show that expenses will sub-

(2) *NH's interest in Grand Central Terminal (GCT) properties.*

By far the largest item in dispute is the value of NH's interest in income derived from hotel and office buildings constructed on property acquired by the New York Central in connection with the construction of Grand Central Terminal (GCT) in New York City and the tracks leading to it.[7] Penn Central contends that, except for repayment of construction advances on the Waldorf Astoria Hotel, $1,110,258 as of December 31, 1966, NH's interest is simply to have the net proceeds of these properties devoted to the payment of terminal expenses; hence when NH ceases to operate its railroad, as it would in liquidation, its interest will end. The bondholders claim NH is entitled to a perpetual half interest in the net proceeds of the properties undiminished by terminal expenses, appraised at $113.5 million, less some $2 million representing the

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stantially exceed receipts in each of the last two years of liquidation, the Trustees would stop at the end of the fourth year and simply abandon the property then unsold. While the studies may be reasonably accurate in total, it would be unrealistic to suppose that the precise timetable of sales would be achieved. Some margin of safety was called for; indeed the Commission may well have been unduly favorable to NH by assuming only a 6-year period. We likewise reject the bondholders' claim that the Commission could not properly adopt the testimony of a witness for the NH Trustees that the property remaining unsold at the end of four years must be discounted by some $8 million for the effect of forced sale; this lay within the field where we must accept determinations supported by substantial evidence.

[7] The reorganization court denied a motion by the bondholders to instruct the NH Trustees to institute a plenary suit for determination of NH's rights in the GCT properties. While in view of the delays in effecting inclusion that have occurred, it might have been better to have followed this course, in light of hindsight, the Commission was required to take the situation as it found it.

amount, capitalized on an 8% basis, of $160,179.22, which on their view of the Agreements, the NH is obliged to pay regardless of its use of the Terminal or a net figure of $111.5 million. The Commission valued NH's settlement prospects at $13 million by a process hereafter described. Since the facts with respect to the contracts and relations concerning the GCT properties are set forth in a painstaking report rendered to the District Court for Connecticut on June 18, by Hon. John Van Voorhis, retired Judge of the New York Court of Appeals, acting as special master, we can condense the recital here. While we have read Judge Van Voorhis' report, we have not relied upon it; our conclusions are our own.

The NH's passenger tracks from the east run only as far as Woodlawn Junction in the Bronx, where they join those of the New York and Harlem Railroad (Harlem), since 1873 a leased line of the New York Central. NH in 1848 acquired trackage rights southward over the Harlem to the latter's terminal, then located at Fourth Avenue and 26th Street; in 1872 the Harlem granted NH and the Central use of the newly built Grand Central Depot. Legislation of 1903 and 1904 required that the tracks immediately north of 42nd Street be depressed below street level; this necessitated demolition of the old depot and construction of the present Terminal.

By agreement of 1907 the Central leased to NH "the use" of the Terminal, not to exceed 50%, in common with the Central. The Terminal was defined as including land and improvements described in annexed schedules, these encompassing certain properties on or in the vicinity of Park Avenue between 42nd and 57th Streets. The Central was bound to acquire all necessary land and to construct the Terminal at its own expense. NH was to pay a proportion,

based on car use, of four items: (i) $485,393.69 interest on the cost of construction of the former depot; (ii) interest, at the rate of 4¼% on the cost of the new Terminal; (iii) annual payments to the City of New York, insurance premiums, taxes and assessments relating to the new Terminal;[8] and (iv) the cost of maintaining and operating it. Section 14 of the lease provided that amounts owing from tenants and others should be collected by the Central, and that "all such rentals or other compensation so received, and not belonging exclusively to either Company, shall be credited to the fixed charges or to the cost of maintenance and operation of the said Railroad Terminal, as the same may be applicable."

Shortly before 1913 it became apparent that large additional revenues could be generated by constructing buildings on land that had been acquired for the Terminal. Desiring "to express more fully the intent of the parties" as to the rights of NH and the Central "with respect to the construction, maintenance and use of such buildings and with respect to the rentals accruing from the leasing of such buildings or portions thereof," the two companies entered into a supplemental agreement in 1913. This added a long paragraph to the section of the 1907 agreement which had originally leased the "use" of the Terminal properties only for the express purpose of accommodating

[8] NH's minimum share of these three items was fixed at $160,179.22. We are unable to share the bondholders' view that the requirement that NH pay this sum regardless of future car use has significant probative value. The minimum payment was exactly equivalent to NH's share of the interest payments due on the construction loans involved in the building of the old depot, and the provision was probably placed in the 1907 Agreement simply to insure that the Central would not be obliged to pay more than its fair share of the cost of the old terminal as a result of building a new one.

the passenger service of the NH. This new paragraph made it clear that the NH also had the right to participate in real estate development, stating that it was

> "agreed that the use of the Railroad Terminal demised by this paragraph to the New Haven Company shall include the right on the part of the New Haven Company to join with the Central Company, in accordance with agreements relating thereto, made, or from time to time to be made, by and between the Central Company and the New Haven Company, in the construction, holding, maintenance and leasing of buildings . . . upon the land included within the Railroad Terminal."

The 1913 Agreement further provided that, as to each building:

> "toward the construction of which the New Haven Company shall furnish or contribute money, and until it is reimbursed therefor, the New Haven Company shall have and own an undivided interest which shall bear the same proportion to the entire building as the amount of money furnished or contributed by the New Haven Company, and for which it has not been reimbursed, bears from time to time to the entire cost for the construction of such building. At the time when the New Haven Company shall be fully reimbursed for all moneys furnished or contributed by it for or toward the construction of any such building, with interest at such rate as shall have been agreed upon, such undivided interest of the New Haven Company shall cease."

Rentals from buildings in which the New Haven participated were to be applied as follows:

"In all cases in which the New Haven Company and the Central Company shall join in the construction of any such building or buildings, the rentals to be credited to the fixed charges or to the cost of maintenance and operation of the Railroad Terminal under the provisions of Paragraph 14 of this agreement shall include all rentals accruing from the leases of the buildings or parts of buildings so constructed, except such rentals as by agreement between the New Haven Company and the Central Company shall be paid either of them as a proper return for the moneys advanced by such party to provide for the construction of any said buildings."

As to many of the buildings constructed NH availed itself of its right to join with the Central, either providing half of the cost or becoming jointly liable to outside institutions supplying the financing; as to three it did not.[9] The rentals from all the buildings after deducting the cost of operation were applied against the expenses of the Terminal except that where NH had not participated only the ground rents were so applied; not until 1964 did these rentals produce a surplus. The NH trustees have sued in the New York courts to recover half these amounts but the actions have not proceeded beyond the pleading stage. Litigation between 1960 and 1962 resulted in decisions by the New York courts that, as to the Biltmore Hotel, a property toward whose construction NH had contributed 50%, NH was entitled to an equal voice with respect to the making of any lease, although the advances had all been repaid. New York Central R. R. v. New York, N. H. & H. R. R., 24 Misc. 2d 414, 208 N.Y.S.2d 605 (Sup.Ct. N.Y. Co. 1960), aff'd,

[9] In the case of the Pan Am Building, the last constructed to date, the tenant supplied all the funds.

13 A.D.2d 309, 216 N.Y.S.2d 928 (1st Dept. 1961), aff'd, 11 N.Y.2d 1077, 230 N.Y.S.2d 226, 184 N.E.2d 194 (1962). The New York courts did not have occasion to determine whether NH was also entitled to an equal share in surplus rentals during its operation into GCT, much less whether any such right would cease on discontinuance. The *Biltmore* litigation had been conducted for NH by Sullivan & Cromwell; in 1964 that firm rendered an opinion to the NH Trustees "that discontinuance of entrances into the Terminal by the New Haven would terminate the 1907 Agreement and the 1913 Agreement as well, except as to the right of the New Haven to be reimbursed for any unpaid building advances."

After reviewing this history the Commission, rejecting the polar positions of Penn Central and of the bondholders, said it would "only decide here that the claims of NH are not frivolous but claims of substance, and in the absence of litigating them they must be deemed to be valuable," 684. It found that, on a relative car-use basis of 40%, NH's share of surplus income would have been $1,842,401 in 1964 and $1,473,627 in 1965—an average of $1,658,014. "Capitalized at 8 percent a year, which we believe to be a realistic rate, this annual average income would have a value of approximately $20 million." Noting Penn Central's concession that NH's claims had a "nuisance value" of $5 million, the I.C.C. apparently averaged these figures for a total of $13 million.

In our view NH's claims to share in the total net income unreduced by terminal expenses and to share in the surplus income differ *toto coelo*. Since the possibility of NH's ceasing operations into the Terminal was scarcely envisioned in 1913, the task of a court now required to determine NH's rights in that event is not so much to determine

what the parties thought but rather to guess, with such small aid as their language gives, what they would have thought if they had.

It is scarcely conceivable that the Central would have agreed that NH, by picking up an option to share in the cost of building hotels or office buildings being constructed for the primary purpose of reducing the heavy expense of operating the Terminal, could quit at any time, take its share of the rentals and leave the Central burdened with the total expense of operating the Terminal, which would not be reduced anything like commensurately by NH's cessation of operations. Whereas only the clearest language would support such a construction, § 14 looks quite the other way.[10] The bondholders argue against this that the Central would receive a windfall if it could apply the rentals from the properties to the expense of operating the Terminal, yet charge a successor of NH its pro rata share of such expense for the privilege of entrance. One answer is that there is on assurance NH will have a successor.

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[10] So too does § 10 which provides that "The compensation to be paid by the New Haven Company for the use of the Railroad Terminal is based upon the fact of the continued use by the New Haven Company of the Harlem Road from the present connection near Woodlawn as an access to the Railroad Terminal. It is agreed that if any * * * new connection eliminates or diminishes the then use of the tracks of the Harlem Company * * *, a new basis of compensation for said Railroad Terminal so long as the same shall be used by the New Haven Company may be demanded by the Central Company, based upon the value of the Railroad Terminal at the time when such connection may be made * * *." If a substantial change in NH operations would permit Central to demand a new basis of compensation, geared to the "value of the Railroad Terminal" at the time, surely the parties did not intend that Central should be left to assume all the costs while NH carried away half of the profits.

Even if the State of New York should acquire NH's tracks from the Connecticut border to Woodlawn in order to maintain commuter service, which is wholly uncertain, it might well elect to operate only to a connection with the New York City subway system rather than bear the heavy expense of an elaborate terminal that was constructed to serve trunk as well as commuter traffic. At least this would be so unless NH were able to pass along its right to enter GCT on what is now an expense-free basis despite the agreement's anti-assignment clause. While that is a possibility, there is no proof that this privilege would so increase the profitability of NH's operations in New York State as to make them more valuable alive than dead. The windfall argument thus comes down to the point that abandonment of NH operations into GCT would reduce the terminal expenses in some amount, not shown of record, and thereby increase the *surplus* income. But here the prospect that the State of New York could acquire NH's right to have the income from the properties applied to terminal expenses, without however raising the price of NH's assets in the state above their liquidation value, works against NH. In short, while Penn Central presumably would pay something to be rid of what we deem an extravagant claim to half the total net rentals, "nuisance value" is not an inapposite expression.

We conclude by the same token that NH's claims to share in surplus income over and above all terminal expenses are exceedingly strong. Just as we cannot imagine the Central's agreeing that the complete dedication of the rentals to payment of the terminal expenses should end on NH's ceasing to operate, we likewise cannot conceive NH's agreeing—or even Central's demanding—that in what would have

been deemed a wholly unlikely event the equally unlikely surplus income should fall entirely into Central's hands. Here also, only the strongest language would lead to such a construction but the only words that would support it—a provision that on reimbursement of advances "such undivided interest of the New Haven Company shall cease"—have been read by the New York courts in the *Biltmore* litigation as subordinate to the language of the granting clause conveying the right to use the land in common with the Central. As to this claim relating to surplus income it is the Central's position that has merely "nuisance value." Hence an allowance of only 65% of what the Commission considered the value of NH's share in the surplus income is "so unreasonable as to require judicial disapproval." Old Colony Bondholders v. New York, N. H. & H. R. R., 161 F.2d 413, 422 (2 Cir.), cert. denied, 331 U.S. 850, 67 S.Ct. 1754, 91 L.Ed. 1865 (1947).

While we are unable to say on this record what the correct figure as to NH's share in the surplus income is, we can indicate our views on certain elements. In the absence of better evidence the 1964-65 experience does not appear unreasonable as a base period unless—which the present record does not tell us although the press does—further projects yielding substantial income are fairly in view.[11] However, Penn Central argues that the Commission er-

[11] The Commission was warranted in refusing to rely on an expert appraisal submitted by the NH Trustees, which estimated that NH would, at an undefined point in the future, earn up to $2.5 million on the properties. The appraisal confessed to being "an optimistic estimate," predicated upon the replacement of the Biltmore, Commodore and Roosevelt Hotels at sometime in the future by large office buildings and their rental on extremely favorable terms.

roneously failed to reduce the "surplus" income to reflect deductible expenditures in those years for hotel equipment and furnishings. It would seem that while deduction of these non-recurring items is appropriate in determining NH's share of 1964-65 income, they should not be deducted in calculating future surplus income unless similar expenses are expectable. In order to entitle NH to the benefits of the agreements, it would have to make the minimum annual payment of $160,000. On the other side we see no basis for determining the NH's share of the surplus income on the ground basis of car-use; when NH participated in building construction, it did so as an equal and should share on that basis. Finally we decline to fault the Commission for its use of an 8% capitalization rate rather than the 5% rate used by the Trustees' expert in estimating the *total* value of the office buildings. The *surplus* income is a marginal item, subject to fluctuation with economic vicissitudes and increased expenses of terminal operation, and a more conservative capitalization rate could thus be deemed in order, especially given the more volatile character of the rentals derived from the hotel properties which the same expert capitalized at 10%. The selection of a capitalization rate, within reasonable limits, is a subject for the expert knowledge of the Commission. While it is argued that the figure of the value of NH's share in surplus income thus determined is subject to discount for the expenses and uncertainties of litigation, Penn Central would likewise have expenses, and also the expense and risk of defending against NH's larger claim. In our view the various items of expense and "nuisance value" wash, leaving the estimated value of NH's claim to half the surplus income not properly subject to reduc-

tion. To this, moreover, there should be added a further sum to reflect NH's interest in surplus income accrued in 1964, 1965 and 1966. All told it would be fair to assume that these readjustments will increase the liquidation value of NH's interest in the GCT properties to at least $25 million.[12]

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[12] Adjustment of the Commission's findings to take into account the NH's right to 50% of the surplus must reflect that in the base years 1964–65, the New Haven was actually receiving a 50% share of an agreed upon portion of the Waldorf Astoria rentals allocated to reimburse the two roads for their construction loans. Thus the increase from a 40% to a 50% share will not increase the NH's interest by a full 25%. While we leave the Commission free to make the actual calculations in light of the best available data and to correct any inadvertent errors on our part, a tentative computation of the value of NH's share in surplus income would run somewhat as follows:

	1964	1965
NH's Share of Surplus As Found by Commission (NHI–49)	$1,320,000	$ 887,000
Adjustment to 50% Basis	340,000	222,000
Total	1,660,000	1,109,000
Reimbursement of Waldorf Loan	523,000	587,000
Total	2,183,000	1,696,000
Average Annual Surplus As Found by Commission	1,658,000	
Adjusted Average Annual Surplus	1,939,500	
Less Guaranteed Minimum Payment to Penn Central	160,000	
	1,779,500	
Capitalized at 8%, Adjusted Value	$22,250,000	

Since NH did in fact receive its share of the Waldorf rents that were allocated to repayment of construction loans, its claim against Penn Central for rents unpaid in 1964–65 is worth approximately $2 million and the total value of NH's claim for accrued but unpaid rents would be around $3 million. Adding this to $22,250,000 would give a figure of at least $25,000,000. This could be argued to be high to the extent that 1964–65 figures were inflated by the New York World's Fair, low to the extent that it fails to include new projects or reflects too conservative a capitalization rate.

(3) *Harlem River and Oak Point Freight Yards.*

The Commission had before it four appraisals of the liquidation value of the Harlem River and Oak Point Freight Yards, a tract of some 160 acres in the southeast Bronx not far from Randall's Island Park. One of the bondholders submitted an appraisal by Mr. Paul O'Keefe, a highly qualified real estate expert, that the best use of the property would be residential and that as such it had value of $32 million. He made another appraisal of $26 million for industrial use. The NH Trustees submitted two reports of Mr. Arthur McCann, valuing the property for industrial use at $22.65 and $18.1 million. Penn Central submitted an appraisal of $15.585 million, also on the basis of industrial use. The Commission took the $18.1 million figure. 668.

Although the bondholders make impressive arguments in support of Mr. O'Keefe's higher figure and we hardly would have faulted the Commission for accepting it, we cannot say there was not substantial evidence for rejecting the appraisal as "at best speculative because of the requirement of a zoning change" since in any event the change "could not be accomplished for some time to come because of outstanding long-term leases held by some of the tenants occupying the premises." Mr. O'Keefe recognized that because of the leases "no assumption • • • can be made that the property can be obtained for immediate residential development." More important, he stated repeatedly that before a zoning change could be approved, an owner must present the city with a development plan for the property. Since he also testified that such a plan could be developed for the yards only if some governmental unit agreed to subsidize housing construction, the Commission

was entitled to consider the possibility too remote to constitute a sound measure of valuation.

On the other hand, we find no adequate explanation in the Report for the rejection of the higher of the two estimates submitted by Mr. McCann, for the New Haven Trustees, or, for that matter, Mr. O'Keefe's industrial use appraisal of $26 million, which in its main discussion of the yards the Commission does not mention. At another point in the opinion, 685, the agency indicated its belief that the earlier and higher McCann study was based upon the assumption that the properties were to be continued to be used as railroad yards and if this were correct, the Commission would have been justified in rejecting it as a guide to the yards' liquidation value. However, we are not at all clear that this understanding was right. Though the summary page of McCann's second and lower valuation study contains a parenthetical statement that the earlier appraisal was made on the basis that the property would be used "as a freight yard of an operating railroad," an examination of the earlier study itself indicates it was not in fact made on that basis but instead assessed the property's "Fair and Reasonable Market Value" to industrial users. The difference in the results of the two studies seems rather to have been due to the second appraisal's having reduced the properties' value by two factors—some $1.825 million in liquidation expenses, and a discount giving effect to the fact that it would take from one to three years to dispose of them. While these are proper enough, the record does not permit us to determine whether they duplicated reductions already made in the Commission's overall calculations. Our remand will enable the Commission to clarify this.

(4) *Boston & Providence.*

A reorganization plan, whereby NH will become the owner of all the B & P's assets, has been approved by the Commission, the courts, In re Boston & Providence R. R. Corp., 260 F.Supp. 415 (D.Mass.1966), cert. denied, 389 U.S. 974, 88 S.Ct. 475, 19 L.Ed.2d 467 (1967), and the stockholders and creditors, and a hearing by the District Court for Massachusetts with regard to confirmation of the plan has recently been held. Since the appraised net liquidation value of the B & P's physical assets was set by the plan at $8.1 million, the bondholders claim that NH's interest should be valued at that figure. The Commission, however, accepted the Trustees' valuation of $4.7 million, which represented the value of the stock carried on NH's books. Both the bondholders and the agency would seem mistaken. Since NH will be obliged under the plan to acquire 20,770 shares of B & P stock now publicly held at a total cost of $2.3 million, this sum should be deducted from the $8.1 million, leaving $5.8 million—$1.1 million more than the Commission's valuation.

In an effort to justify the $4.7 million figure the Commission and Penn Central point to another feature of the reorganization plan which is claimed to reduce the value of the B & P stock to NH. When the B & P plan was approved by the Commission, there was thought to be substantial possibility that parts of its roadway might be sold to the Massachusetts Bay Transit Authority or be taken by that or some other governmental agency for highway purposes at prices substantially in excess of their appraised value under the reorganization plan. To take this into account, the plan provides for the issuance of Certificates of Contingent Beneficial Interest (CCBI's) as to the proceeds of any such sale, involving more than $500,000,

which occurs before December 31, 1978. 48% of the CCBI's are held by the New Haven, 52% by other ex-shareholders. The Commission argues that because NH will be obliged to pay out 52% of the net proceeds of such sales without a deduction for the value of the properties already credited in the reorganization proceedings, the agency was justified in deducting the $1.1 million. Apart from the fact that the Report does not rely on this as the basis for the discount, it seems highly questionable, particularly in light of current market assessments of the value of the CCBI's, that any reduction is justifiable.

Before leaving liquidation value, we should discuss some of the bondholders' many criticisms we do not accept. Foremost among these is the Commission's failure to allow for "going concern" value. The bondholders submitted an estimate that a rebuilding of NH would require some $55 million for such intangibles as market investigations, organization costs, engineering expenses, and interest during construction. The agency said this estimate was vastly overstated, finding that, at most, 10% of the figure was justified. It refused to credit the estate even with this lesser sum, however, on the ground that "[i]t is not realistic to assume that a potential buyer would pay the liquidated value of the NH assets and then pay additional amounts representing elements of going concern value in the face of NH's past deficit operations and its bleak prospects for the future." 687. We agree. Broadly speaking, there is no "going concern value" in a deficit ridden railroad being liquidated as real estate or scrap; the bondholders cannot have it both ways. The argument has slightly more force—but not enough to persuade us—when presented in a much more limited form. It is possible, perhaps even likely, that rather than suffer termination

of service, some of the states would condemn parts of NH's operating properties, and the bondholders rely on a recent decision of the New York Court of Appeals, Port Authority Trans-Hudson Corp. v. Hudson Rapid Transit Tubes Corp., 20 N.Y.2d 457, 472, n. 4, 285 N.Y.S.2d 24, 33 n. 4, 231 N.E.2d 734 n. 4 (1967), as requiring payment for "going concern" values regardless of anticipated losses in such event. However, that case dealt with a unique situation where the larger part of the property being condemned, tunnels under the Hudson River, had no value for any purpose save that for which they were being taken and though there are dicta supporting the bondholders' position, it is at least doubtful that the rule would be applied in other situations in which the condemnee's equities were not so compelling. Certainly federal law does not require payment of going concern value in condemnation when liquidation constitutes a property's "highest and best" use since the assets have substantial value for that purpose but no earning power. See 2 Orgel, Valuation Under Eminent Domain § 194 at 41 (1953). Kimball Laundry Co. v. United States, 338 U.S. 1, 69 S.Ct. 1434, 93 L.Ed. 1765 (1948), upon which the bondholders mistakenly rely, makes it clear that "going concern value" must be allowed only when there is reason to believe that as a result of investment in intangibles, the earning capacity of the enterprise is greater than is "commonly * * * given to such a combination of land, plant and equipment." Id. at 9, 69 S.Ct. at 1439. Consequently, the states would not be compelled to resort to condemnation since the I.C.C. could constitutionally condition any certificates of abandonment issued to NH on its agreeing to sell its assets at their scrap value to a purchaser intending to operate the properties as a railroad, as it has done in similar situations in the past.

See, e.g., Jay Street Connecting R. R. v. United States, 174 F.Supp. 609, 617 at n. 2 (E.D. N.Y. 1959).

Somewhat similar considerations apply to the bondholders' contentions that the Commission should have included tax benefits to Penn Central in computing NH's liquidation value. These are of two different sorts. As to one, large loss carry-forwards, amounting to $82.7 million as of December 31, 1965, realization will depend on Congress' enacting legislation which the Treasury Department has opposed. The other lies in the potential for increased depreciation allowances and, on sales or abandonments of assets, either increased loss deductions or reduced capital gains arising from the excess of NH's tax basis for its properties over their cost to Penn Central. This is subject to some legal doubt, and the value of both types of benefit is also rendered uncertain by the large reservoir of tax deductions already available to Penn Central. What is decisive, however, is that benefits of this kind do not fit the notion of liquidation value. Since NH could not pass such benefits on to persons buying its property on a piecemeal basis, it is not entitled to have them added to liquidation value for purposes of sale to Penn Central, as it would be if the properties were being valued on an operating basis, cf. Erie-Lackawanna R. R. v. United States, supra, 279 F.Supp. at 346. The only consideration appropriate for these items under the circumstances is in somewhat reducing the cost of the acquisition to Penn Central.

For different reasons we decline to fault the Commission for rejecting the testimony of an expert witness for the bondholders that the Trustees' liquidation study did not take into account that little or no expense would be entailed in the sale of substantial sections of NH's lines since these "would be candidates for purchase by other carriers."

While the point is appropriate, the witness was uncertain both as to what segments would prove to be successful "candidates" for sale "in place" and the prices at which such sales would be made. He concluded only that the Trustees' estimate was "substantially understated," without committing himself to the dollar amount of the adjustment allegedly required. The Commission was justified in not undertaking an assignment the witness had declined, especially since "the simple fact is that no other railroad has displayed an interest in purchasing any portion of NH." 679. The bondholders' criticisms of a variety of other findings—notably, the values assigned by the Commission to NH's investments in cooperative undertakings with other railroads and to passenger cars—must be rejected as seeking to have us invade the Commission's province.

IV. *The Value of the Consideration to be Received.*

The Commission placed the following values upon the property to be received by NH under the Purchase Agreement:

	Millions
(1) 950,000 shares of Penn Central stock at $87.50 a share	$ 83.1
(2) $23 million principal amount of Penn Central 5% bonds	20.0
(3) Assumption by Penn Central of Boston & Providence mortgage	3.0
(4) Purchase Price Adjustments Under Purchase Agreement	9.5
(5) Cash	8.0
	123.6

The bondholders assail items (1) and (4) as too high; they also contend the computation failed to take into account that $16.2 million of the price may have to be used to pay accrued real estate taxes in order to permit the conveyance free of liens which the Purchase Agreement requires. We reject the first criticism but sustain the other two.

The bondholders say there was no adequate basis for valuing Penn Central stock at $87.50 a share, when at the time of the I.C.C.'s decision, Pennsylvania stock—which was to be exchanged on a one for one basis for new Penn Central common—was being traded in the $60 range. In defense of its higher figure, the Commission cites the testimony of William J. Kirk, one of the NH Trustees, who stated that in concluding the Purchase Agreement he assumed the stock's price would be fluctuating between $75 and $100 at the time of the closing. 688-89. As his testimony does not reveal the basis for this belief, the Commission sought to establish that a proper analysis of Penn Central's prospective earning power led to a similar conclusion. It first capitalized at 8% the net income earned by the Pennsylvania and the Central separately in 1965 and thus concluded that the value of a Penn Central share, before considering merger savings, was $68. It then capitalized the $81 million in annual savings anticipated from the merger, subtracting only the $8.5 million it expected NH to lose annually after inclusion, thereby arriving at post-merger earnings of $8 per share, and concluded that the "inherent quality" of the stock demanded a price of $100, thus indicating that its $87.50 estimate was fair. Against this it is urged that the Commission's calculations overlook that the annual savings of $81 million were not expected to be attained until eight years after the merger

was concluded, Pennsylvania R. Co.—Merger—N. Y. Central, 327 I.C.C. 475 at 501 (1966), with a great part of them dependent upon the completion of a four year modernization program. Id. at 489-90.[13]

While this complaint might have considerable validity if the Commission had valued the Penn Central stock at $100 per share, that is not what the Commission did. If $72.5 million of annual net savings would raise the market price from $68 to $100, only some $45 million would be needed to raise this to $87.50. When the stock market's tendency to look to future earnings is borne in mind, it was not unreasonable to estimate that a price of $87.50 would be realized by the time of the closing—assuming that normal market conditions then prevailed. The increase in the price of the stock to around $85 per share at this writing at least shows that the Commission's figure is not wild speculation.

The bondholders assert also that there was no occasion to indulge in any guessing as to the value of the Penn Central stock since the I.C.C. could simply have required issuance of such number of shares, taken at average stock market prices over a period before the closing, as were needed to produce the desired total price. Due to the cyclical nature of the railroad industry this might operate quite unfairly. While if Penn Central had had a history extending over a cycle, an average during such a cycle might have been fair, no such experience was available.

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[13] The bondholders argue also that the merger savings will be, indeed to a considerable extent already have been, dissipated by wage increases. The Commission was warranted in refusing to accept such a defeatist view. Compare Erie-Lackawanna R.R. v. United States, 279 F.Supp. at 341.

On the other hand, the Commission's treatment of the consideration to be paid in satisfaction of Penn Central's obligations under the "Purchase Price Adjustment" provisions, item (4), must be regarded as erroneous. Penn Central has the right to make this payment either in cash, stock or in 5% bonds. While the agency recognized that the $23 million of Penn Central bonds that the New Haven is to receive would not be worth par and therefore valued them at only $20 million, it did not apply a similar discount to the bonds of the same type which Penn Central can use to satisfy its obligations under the "adjustment" clause. We find no force in the response that since Penn Central has the option to pay this sum in cash or stock, the I.C.C. could not assume that payment will be made in bonds. It is apparent that Penn Central will choose the cheaper way out. The Commission's appraisal is thus overstated by $1.3 million.

We likewise see no sufficient answer to the bondholders' contention as to the failure to make a deduction for the $16.2 million of accrued real estate taxes on property required to be transferred free of liens, which, they say, resulted either in an overstatement of the consideration to be received by the estate or an understatement of liquidation value. The Report does not discuss this and only Penn Central seeks to justify it, on the basis that the reorganization court can direct a sale free of liens and it may thereafter be possible to persuade state and local taxing authorities to accept a reorganization plan providing less than full satisfaction for their claims. But even if part of the taxes were forgiven, the effect of the error would not be corrected. For the agency deducted the full $16.2 million when calculating the Estate's net liquidation value.

Before considering the third of the Commission's calculations, the cost of the acquisition to Penn Central, we should examine whether the Commission made errors in the direction of overstating NH's liquidation value that would reduce or eliminate what may be a discrepancy exceeding $45 million between that figure and the value of the consideration to be received.[14] Only two of those suggested warrant discussion. The Commission's brief takes a deduction of $3 million for 1966 depreciation. This item is not found in the Report and its derivation is obscure. A much more significant item is raised by the claim that before the NH Trustees could even begin a liquidation, lengthy abandonment proceedings would be required, during which large cash losses would be incurred and the property would further depreciate. The bondholders respond that if inclusion of NH in Penn Central had not been in prospect, the NH Trustees would have been under a duty to initiate abandonment proceedings as soon as they reported, on December 31, 1963, that there was no prospect for independent operations of NH, and that

[14] The derivation of this is as follows, it being understood that all figures are approximate only:

	Millions
Liquidation value as found	128.9
Plus Discount of expenses to present value	6.
G.C.T. properties	12.
Bronx freight yards	4.5
Boston & Providence	1.1
Adjusted liquidation value	152.5
Value of consideration as found	123.6
Less reduction in purchase price adjustments	1.3
	122.3
Less allowance for taxes	16.2
Adjusted value of consideration	106.1

December 31, 1966 is thus an entirely reasonable date for the beginning of the assumed liquidation. Indeed, they insist they are entitled to be fully protected against losses thereafter—a contention we shall discuss below. Our rejection of that contention, see section VII of this opinion, means that a considerable portion of the losses will be borne by the NH estate, and there would be no justification for a double deduction. Beyond that, the Commission had to pick a date for valuation and December 31, 1966 was a reasonable choice. If we were to posit a liquidation beginning only some years hence, we could not simply deduct interim cash losses and depreciation but would have to ask the Commission to revalue the assets and this might yield a higher price. 698.

V. *Cost of Acquisition of NH to Penn Central.*

The Commission found the cost to Penn Central of acquiring the assets of NH to be as follows:

	Millions
(1) 950,000 shares of Penn Central stock at $87.50 per share	$ 83.1
(2) $23 million principal amount of Penn Central 5% bonds	23.0
(3) Assumption by Penn Central of Boston & Providence mortgage	3.2
(4) Purchase Price Adjustments under Purchase Agreements	9.5
(5) Cash	8.0
(6) Equipment obligations	22.6
(7) Labor protection and pension costs	9.0
	$158.4

We have concluded above that the Commission's determination of item (1) was within the powers accorded to it. While items (2) and (3) also find their analogues in the computation of the value of the consideration to NH, the Commission here priced them differently—taking the face value of the bonds rather than their estimated value at the time of closing, on the basis that Penn Central would ultimately have to pay this. We find this unpersuasive; no one would regard the issuance of a long term noninterest bearing note as costing the issuer the face amount, and the same principle covers a bond carrying an interest rate below that necessary to enable it to sell at par. Items (2) and (3) should thus be reduced to $20 million and $3 million respectively and, for reasons indicated above, item (4) should be reduced to $8.2 million.

The bondholders' attack on item (6) may have merit. A substantial proportion of New Haven's equipment, valued at $8.7 million, stands as collateral for $14.3 million in equipment loans. Another substantial portion, valued at $28.8 million, stands as security for only $10.1 million in loans. The bondholders argue it was unreasonable to believe that Penn Central will assume $14.3 million in equipment obligations to get the continued use of $8.7 million in equipment, when under the Purchase Agreement it can require the NH Trustees to disaffirm these obligations. The Commission held, however, that the Penn Central would assume all the equipment obligations since the equipment is "required to continue NH operations." 693. The Report does not satisfy us that the Commission fully understood the bondholders' argument; Penn Central might itself have surplus equipment or be able to get it from other sources more cheaply than by assuming obligations 165% of the

equipment's worth. Unless there is some better explanation why Penn Central would follow such a seemingly ill advised course, the cost to Penn Central should be reduced by $14.3 million less the cost of additional equipment that must be secured to replace NH equipment that would be repossessed.[15] On the other hand, we are not persuaded that the Commission overstated item (7).

As against the items where some reduction in the cost of acquisition to Penn Central is demanded, much larger ones were omitted. One of these is Penn Central's compulsory participation in NH's losses from the consummation of the Penn Central merger, 717-19, which, if NH's inclusion should take three years, will amount potentially and, very likely, actually to $16.5 million even on the Commission's formula. Moreover, we do not see why the burden of future NH losses, estimated by the Commission at $8.5 million after economies from consolidation should not likewise be considered a cost from a practical although not an accounting standpoint. Capitalized at an 8% basis this would amount to an additional $106 million. We thus find the total cost of the acquisition of NH to Penn Central under the arrangements approved by the Commission will exceed $250 million. This figure must, of course, be evaluated in light of the ultimate $72.5 million annual savings from the Penn Central merger after allowing for NH losses —a value of some $900 million, capitalized on the same basis.

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[15] An additional adjustment will be required to take into account the fact that the total amount of the equipment obligations had been reduced from $24.4 million as of December 31, 1965—the time at which the Trustees' expert analyzed the problem—to $22.6 million as of December 31, 1966—the date of the Commission's valuation.

VI. *The Effect of our Redetermination on the Commission's Order.*

In our view the Commission's finding "that the consideration is at least equivalent to the liquidation value," 697, could well be erroneous in the $45-50 million range. Hence the consideration may be only some two-thirds of liquidation value. We must now decide what the consequences of that error are.

Citing some or all the passages from the Report we have quoted at the outset of this opinion, the defendants argue that the Commission never said that NH must receive liquidation value, and that any such statement would be bad law. Agreeing there are passages in the Report that lend support to the former contention, we find the argument insufficient to avoid the need for a remand. This is not a case in which the agency, while understanding the basic outlines of the problem before it, explains the grounds for its decision inadequately, Phelps Dodge Corp. v. N.L.R.B., 313 U.S. 177, 196-197, 61 S.Ct. 845, 85 L.Ed. 1271 (1941), or unsoundly, SEC v. Chenery Corp., 318 U.S. 80, 63 S.Ct. 454, 87 L.Ed. 626 (1943). In finding that the consideration was the equivalent of NH's liquidation value, the agency misapprehended the facts. While remand would not be required even in such a case if the improper findings could justly be considered subsidiary unless there is "solid reason to believe that without the subsidiary finding the agency would not have arrived at the conclusion at which it did arrive," Communist Party of United States v. Subversive Activities Control Board, 367 U.S. 1, 67, 81 S.Ct. 1357, 1395, 6 L.Ed.2d 625 (1961), here the agency's mistake went to the heart of its analysis. We cannot be certain that if the Commission had known of its errors of fact,

it would have approved the price provided by the Purchase Agreement, even if it had held the views of the law the defendants now attribute to it. This being so, we must send the case back. See Braniff Airways, Inc. v. CAB, 126 U.S.App.D.C. 399, 379 F.2d 453, 465-467 (1967) (Leventhal, J.); NLRB v. Reed & Prince Mfg. Co., 205 F.2d 131, 139 (1st Cir.), cert. denied, 346 U.S. 887, 74 S.Ct. 139, 98 L.Ed. 391 (1953).

While we could end this section of the opinion at this point, we think it will be useful to indicate our views as to the proper legal standard. There is some initial appeal in the position that when the cost of the acquisition of NH to Penn Central under the Purchase Agreement, including capitalization of future losses, will exceed the NH's liquidation value by $100 million, the Commission is not required to make Penn Central pay still more; the price, it is said, must be reasonable to the buyer as well as the seller. But this ignores the constitutional right of NH to cease operation and liquidate. We see no reason to question the validity of Justice Holmes' decision in Brooks-Scanlon Co. v. Railroad Commission, 251 U.S. 396, 40 S.Ct. 183, 64 L.Ed. 323, forbidding the State of Louisiana to require a railroad to continue its deficit operation with no hope for profits in the foreseeable future. See also, Mora v. Mejias, 223 F.2d 814 (1 Cir. 1955); Railroad Commission v. Eastern Texas R. R., 264 U.S. 79, 85, 44 S.Ct. 247, 68 L.Ed. 569 (1924); Bullock v. State of Florida ex rel. Railroad Commission, 254 U.S. 513, 41 S.Ct. 193, 65 L.Ed. 380 (1921); cf. Pacific Telephone & Teleg. Co. v. Tax Comm'n, 297 U.S. 403, 413, 56 S.Ct. 522, 80 L.Ed. 760 (1936). We cannot accept the argument that all this was changed by the addition of § 1(18), requiring the Commission's consent

to abandonment, to the Interstate Commerce Act by the Transportation Act, 1920, or by the enactment of § 77 of the Bankruptcy Act in 1933. These statutes were designed to assure orderly procedures and to afford methods that might avoid the ultimate solution; they were not intended to override constitutional guarantees,[16] cf. In re Third Avenue Transit Corp., 198 F.2d 703, 707 (2 Cir. 1952), and would not be effective if they had been. In the usual case under § 5(2) (d) the Commission doubtless is not *required* to fix a price as high as the road to be acquired might obtain elsewhere if its value to the acquiring road will not be that great, although we have intimated that it *could* lawfully do so on a showing that inclusion was required by the public interest and that this was the only way to meet the owners' "reasonable expectations, perhaps based on inclusion in another system that would be less in the public interest." Erie-Lackawanna R. R. v. United States, supra, 279 F.Supp. at 338. But when the asking price for the

[16] We find no such indication in the provision of § 77(b) (5) that a plan of reorganization "shall provide adequate means for execution of the plan, which may include * * * the sale of all or any part of the property of the debtor either subject to or free from lien at not less than a fair upset price." The last phrase referred to the practice that had grown up in railroad receiverships whereby the court gave some protection to non-assenting bondholders by setting a minimum price which the trustee or committee representing holders of bonds whose lien was being eliminated must bid. See Spring, Upset Prices in Corporate Reorganization, 32 Harv.L.Rev. 489, 493–94 (1919); Weiner, Conflicting Functions of the Upset Price in a Corporate Reorganization, 27 Colum.L.Rev. 132, 137–44 (1927); 6 Collier, Bankruptcy, ¶ 0.04 [2.2] (1965). Since such proceedings looked to continued operation, the question whether bondholders were entitled to liquidation value did not arise. We find nothing in Ecker v. Western Pac. R.R., 318 U.S. 448, 468, 63 S.Ct. 692, 87 L.Ed. 892 (1943), cited by the Commission, which bears on the problem.

acquired road is what the Constitution demands the owners must receive as a condition to allowing the road to be operated in the public service, we think—subject only to what we shall say hereafter as to interim losses—that the Commission may not fix, or approve, anything less.

We recognize, however, that this legal issue is one of novel impression which only the Supreme Court can authoritatively determine. We therefore suggest in the interest of avoiding another remand that if the Commission disagrees with our view, it should feel free to formulate its own and supply the necessary subsidiary findings. The Commission is therefore directed to make detailed findings as to each element of liquidation value and of the consideration to be paid by Penn Central on a basis consistent with this opinion.[17] If it agrees with our view that the price cannot be less than the liquidation value, it shall prescribe suitable terms. If it does not, it shall state the pricing theory it has adopted, the reasons for it, and the results, and shall make whatever detailed subsidiary findings are required to support this.

VII. *The Claim of the Trustee of the Harlem River Division Mortgage for Assumption.*

United States Trust Company (USTC), Trustee of NH's Harlem River Division First Mortgage, raises a special point. The mortgage, which secures $6,647,000 outstanding 4¼% bonds, on which there was accrued and unpaid interest of $1,694,935 as of December 31, 1966, is a first lien on

[17] We suggest that these findings be in such detail that if the Supreme Court should disagree with our rulings on specific issues, it will be able to make, or direct us to make, the necessary adjustments.

the line of railroad extending from the Harlem River and Lincoln Ave. in the Bronx some 11.5 miles to New Rochelle, N. Y., where it connects with NH's line from Connecticut to Woodlawn, N. Y. The mortgaged line, an integral part of the through Hell Gate Bridge route to Pennsylvania Station and thence to points to the south and west, includes the two large freight yards discussed in Section II(3) of this opinion. USTC asserts, and no one has denied, that even on the Commission's figures, which it regards as too low, the net liquidation value of property subject to the lien of the Harlem River Division mortgage is nearly $23 million. The Purchase Agreement gives Penn Central the option to assume the Harlem River Bonds; if it does, its obligation to issue $23 million of 5% first mortgage bonds will be reduced by the principal and accrued interest on the Harlem River Bonds so assumed.

USTC claims it is unfair that the Harlem River bondholders should be left dependent on Penn Central's decision. It says that, alone among NH's bondholders,[18] those under the Harlem River mortgage are fully secured, and that it would be inequitable to deprive them of their lien and leave them only with a right to assert priority over other NH bondholders in the proceeds of the sale. It cites, as an instance of what might lie ahead, the proposal in the NH Trustees' Plan of Reorganization that the Harlem River bondholders accept a package consisting of seven year 4¼% subordinated debentures, secured in main part

[18] As a result of the prior reorganization, 254 I.C.C. 405 (1943), NH's once complex mortgage structure has become simple. The First and Refunding Mortgage is a first lien on the entire property subject only to the prior lien of the Harlem River mortgage which was left undisturbed, id. at 449-50; the General Income Mortgage is junior to the First and Refunding, id. at 439.

by Penn Central common stock, for the principal of their claim, and even more speculative NH common stock for the accrued interest. USTC finds the Commission's refusal to order assumption of the Harlem River bonds by Penn Central particularly frustrating in light of the lack of objection by anyone.

While there is much force in USTC's position, we think its request deals with a matter better left to the reorganization court. There is no reason to believe that the District Court for Connecticut would approve a plan that did not provide fairly for the Harlem River bondholders. See Group of Institutional Investors v. Chicago, M., St. P. & P.R.R., 318 U.S. 523, 564, 63 S.Ct. 727, 87 L.Ed. 959 (1943). While that court does not have the power that we do, in reviewing the Commission's order under § 5 of the Interstate Commerce Act, to require a change binding on Penn Central, it has ample means to see to it that fair provision is made for the Harlem River bondholders and we would not wish to impinge on its freedom of action.

VIII. *Protective Conditions and Loss Sharing.*

The NH bondholders contend the Commission erred in not requiring an immediate takeover of NH by Penn Central, in the form of a lease or otherwise; that the arrangements for a $25 million loan and sharing in losses which the Commission prescribed as a substitute are unfair; and that the Commission should have imposed "Appendix G" financial conditions for the benefit of NH similar to those it stipulated in favor of Erie-Lackawanna, D & H, and B & M. See 259 F.Supp. at 970-971; 279 F.Supp. at 326-329.

Our last opinion recounted the steps taken by the Commission through September 1967, to keep NH alive pend-

ing its inclusion in Penn Central, 279 F.Supp. at 332-335. In the Report the Commission adhered to its refusal to direct inclusion of NH in Penn Central without the terms having been fixed by it and passed upon by the reorganization court and found itself convinced "that a quick takeover in this case could not be accomplished by means of a lease," 705—views it was justified in holding. It prescribed a $25 million loan with provisions for loss-sharing by Penn Central, and evidently concluded that with these arrangements in effect there was no need for Appendix G conditions. The loan can be taken down whenever the NH Trustees' cash balance falls below $5 million. It is to be evidenced by Trustees' certificates bearing interest at the prime rate of Morgan Guaranty Trust Co. at the time and maturing December 31, 1971; these can be retained, sold or applied toward the price of acquiring the NH assets, except insofar as they have been cancelled under the loss-sharing formula. This begins with the deficit in net railway operating income. That sum is to be decreased by any income from the GCT properties which Penn Central agrees to pay NH, by depreciation which Penn Central bears in any event under the Purchase Agreement, and by retirement losses. Of the deficit thus adjusted, Penn Central is to bear 100% in the first year after the Penn Central merger, 50% in the second year, and 25% in the third, but in no event more than $5.5 million in any year.

The broadest position of the NH bondholders is that Penn Central should have been required to shoulder 100% of the losses for whatever period is needed to effectuate inclusion of NH or, for that matter, until abandonment is authorized if inclusion should prove impractical. This position stems from the considerations developed and to some extent approved in Section VI of this opinion. The

bondholders were entitled, they say, to have the NH Trustees begin abandonment proceedings in 1963 when the Trustees reported that future operations of NH as an independent railroad were unfeasible; that the Trustees failed to do this only because inclusion of NH in Penn Central appeared to offer an alternative preferable in the public although not in the bondholders' interest; that the Commission found the Penn Central merger to be in the public interest only if NH were included; and that it would thus be inequitable—indeed unconstitutional—if the liquidation value of NH as of December 31, 1966, were to be eroded by losses "which reduce the value of the assets or represent deferral of expenses that have a prior claim on the NH estate," 703-04, n. 33. Supporting the Commission's course Penn Central argues against this that a considerable part of the losses could be avoided if NH could be immediately included in Penn Central; that Penn Central cannot fairly be penalized for NH's inability to consummate the inclusion more promptly; and that to impose all the losses on it would encourage the NH bondholders to litigate endlessly. It adds, properly in our view, that the Commission's statement, 327 I.C.C. at 524, that the Penn Central merger would not be consistent with the public interest "without complete inclusion of NH" is by no means the same as saying it was only the inclusion of NH that rendered the merger in the public interest; the statement rather must be read along with the Commission's finding, that, absent inclusion, Penn Central "with new routings and improved service, could undoubtedly wean substantial traffic away from NH and leave that already moribund carrier in perhaps an irretrievable situation." 327 I.C.C. at 522.

While we do not find choice between these positions easy, we accept the Commission's view that it was not

bound to require Penn Central to assume all losses of NH subsequent to the Penn Central merger. No one seriously questions that the NH Trustees made the right choice in pressing for inclusion in Penn Central rather than in seeking permission to abandon. To say they should have pursued the two paths simultaneously ignores the limits on human energies and on the Commission's time. If the Trustees had presented abandonment applications as an alternative to sale, the Commission would almost certainly have deferred their consideration for a reasonable period while inclusion was being explored. If inclusion had been found impracticable, the NH bondholders would have had to shoulder losses between the date of such a determination and the grant of authority to abandon. We cannot see why the contrary result entitles them to have the entire burden of such losses shifted to Penn Central. Although we agree that by investing in a railroad the bondholders did not surrender their constitutional right not to be required to operate the property at a perpetual loss, they did subject themselves to such interim losses as are reasonably incident to working out the solution most consistent with the public interest. See Meyers v. Jay Street Connecting R. R., 259 F.2d 532 (2 Cir. 1958), and 288 F.2d 356 (2 Cir.), cert. denied, 368 U.S. 828, 82 S.Ct. 49, 7 L.Ed.2d 31 (1961). Cf. Palmer v. Commonwealth of Massachusetts, 308 U.S. 79, 89, 60 S.Ct. 34, 84 L.Ed. 93 (1939).

If we are right in this, the Commission was justified in setting a ceiling on Penn Central's participation in losses and in providing that it bear only a fractional share. The NH bondholders say that even if this be true, the downward progression of Penn Central's percentage constitutes an *in terrorem* provision designed to thwart them from fully presenting their claims to fair treatment. We agree

that desire to curtail litigation is an insufficient reason for the downward progression. The Commission should not have assumed that the bondholders' attacks would necessarily lack merit; indeed this opinion shows the contrary. Moreover Penn Central has as much opportunity as the bondholders to prolong litigation. Since the Commission expressly placed the downward slide on this basis, the formula cannot stand, see Justice Douglas' dissent in the Penn-Central Cases, 389 U.S. at 557-558, 88 S.Ct. 602, and we must remand for reconsideration. In doing this we in no way suggest that the agency is obliged to place more of the burden upon Penn Central unless, upon further reflection, it concludes that either the Constitution or equity so requires. It is not barred, for example, from following an ancient precedent and splitting the losses in half, despite the fact that its original formula required Penn Central to accept 58⅓% of the anticipated losses if inclusion should take three years and 75% if it comes at the end of the second year, assuming that the losses do not increase. Another formula perhaps meriting consideration would be to gear the portion of the losses not assessable against Penn Central to the savings it could accomplish if inclusion had been effected. It could well be, however, that still further analysis is required. The original loss sharing formula, limiting Penn Central's burden in any year to a maximum of $5.5 million, was clearly predicated upon the agency's view that NH's fortunes had reached their nadir in 1967 and that the outlook for 1968 and beyond was somewhat less dismal 718-19. The Commission is free to consider, in the light of more current information, whether this assumption is correct. Similarly the Commission's confidence that the $25 million loan will provide for NH's cash needs

pending inclusion may prove misplaced. It follows from the principle of those cases remanding administrative decisions because of staleness of the record[19] that where, as here, remand of an issue is required on other grounds, the Commission should not be prevented from taking steps to protect the public interest by virtue of an earlier failure to predict the future accurately. Consequently, if additional funds are required to assure NH's continued operation pending inclusion, the agency should take steps to avoid the danger by appropriately recasting these provisions.

There remains the contention that the Commission was bound to prescribe Appendix G type conditions for the protection of NH. We have previously expressed our view that there was no real analogy between the three roads benefitting from such conditions, whose future relationship with Penn Central was almost certain to be highly competitive, and NH, the Pennsylvania's historic connection to New England and now to be made a component of the Penn Central system. See Oscar Gruss & Son v. United States, 261 F.Supp. at 389-391. We have also said, that "The unlikelihood that Penn Central would avail itself of its opportunities for diversion from NH in the interval prior to inclusion would be heightened if it is now required

[19] Atchison, Topeka & S. F. Ry. v. United States, 284 U.S. 248, 52 S.Ct. 146, 76 L.Ed. 273 (1932); Marine Transp. Lines, Inc. v. United States, 173 F.Supp. 326 (D.D.C.1959); State of Oklahoma By and Through Corporation Comm. v. United States, 193 F.Supp. 261 (W.D.Okl.1960). Cf. Northeast Airlines, Inc. v. CAB, 345 F.2d 484 (1 Cir. 1965). See generally Freedman, The Uses and Limits of Remand in Administrative Law: Staleness of the Record, 115 U.Pa.L.Rev. 145 (1966). See also, Secretary of Agriculture v. United States, 347 U.S. 645, 654–655, 74 S.Ct. 826, 98 L.Ed. 1015 (1954).

to bear or share in operating losses." Erie-Lackawanna R. R. v. United States, 279 F.Supp. at 336. It appears also that a major rerouting of traffic between New England and points west of Albany, which is indeed in contemplation, depends on the completion of a new yard at Selkirk, N. Y. some years off. Furthermore Appendix G financial conditions might be quite unfair to Penn Central when applied in favor of a road whose freight revenues are deteriorating for reasons wholly unrelated to the Penn Central merger. Under all the circumstances we cannot say the Commission acted arbitrarily or capriciously in refusing to impose Appendix G conditions.

IX. *Protective Traffic Conditions for Erie-Lackawanna at Maybrook, N. Y.*

NH has long maintained an important interchange of New England freight traffic with two sets of carriers at Maybrook, N. Y.—the route from Maybrook crossing the Hudson River at Poughkeepsie and joining NH's main line at New Haven. One group, comprised of the Central Railroad of New Jersey (CNJ), the Reading and the Western Maryland, provided service to and from points in southeastern Pennsylvania and western Maryland and beyond, which competed primarily with the service furnished by the Pennsylvania via New York harbor. Erie-Lackawanna (EL) supplied service through Binghamton, N. Y. and beyond, competitive both with the Pennsylvania and with the New York Central's service through Albany.[20] The EL con-

[20] Further competition is furnished by the B & M's interchange with D & H at Mechanicsville, N.Y.—the D & H connecting with El at Binghamton and, under the Penn Central merger decision, 327 I.C.C. at 527–28, to have trackage rights from Wilkesbarre, Pa. to a connection with N & W at Hagerstown, Md.

nection has been exceedingly important, 124,435 cars having been handled with it via Maybrook in 1966 as against no more than 97,391 with CNJ (51,228 via Maybrook); and 102,980 handled by NH and Pennsylvania via New York harbor. NH has solicited preferentially for the Maybrook gateway since this generally affords its longest haul, and has worked cooperatively both with CNJ, Reading and Western Maryland and with EL to develop excellent service and connections.

At the request of CNJ, Reading and Western Maryland, the Commission imposed in their favor special traffic conditions, set forth in Appendix I to its Report, 752-53, to maintain the quality of service and equality of solicitation for the Maybrook interchange pending decision on the application for inclusion of these lines in a proposed N & W-C & O system.[21] However, it denied a similar request by EL. Noting Penn Central's contention that "EL is really seeking a built-in competitive advantage for itself and the N & W system," 738, the Commission stated:

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[21] The Commission said, 736:

> "In these circumstances, C & O–B & O, third and smallest of the major eastern carriers, assuming consummation of the Penn-Central merger and inclusion of EL, D & H, and B & M in the N & W system, would be left without an equivalent access route into New England. Penn-Central would have Selkirk and B & A, N & W would have Mechanicsville, N. Y., and B & M. In the face of such competition and without a competitive gateway into New England, the ultimate impact on the intervenors could be serious and detrimental to the shipping public, which would lose an effective choice of the C & O–B & O family lines service to and from the NH territory. If intervenors were to be included in the N & W system as is contemplated in the application in the N & W–C & O case the need for this third gateway to New England may end. Therefore, we shall impose protective conditions pending decision in that case."

By imposing conditions of the type suggested, we would not be merely sustaining a necessary operation until it could fend for itself, but we might well be creating a permanent division of markets with undesirable effects on the competition.

It should be noted that N & W has not requested the imposition of any conditions in this proceeding. Evidently, through prescription of the conditions it has proposed, EL hopes to gain some protection against N & W adopting a policy of employing the Mechanicsville gateway to and from New England and thereby short-hauling EL. Penn-Central should not have to shoulder the responsibility of safeguarding EL from its parent. In any event, so long as the conditions imposed to protect CNJ, Reading and WM remain in effect, they would also benefit EL.

EL petitioned for reconsideration. In its Third Supplemental Report, rendered March 1, 1968, the Commission denied this without prejudice to EL's renewing the application on the basis of actual experience of injury. The Commission amplified the reasons previously given, as follows:

(1) EL would have the benefit of the standard routing conditions set forth in Appendix I of the initial report approving the Penn Central merger, 327 I.C.C. at 564, 565.

(2) The special conditions imposed for the benefit of CNJ; Reading and Western Maryland "will redound to the benefit of EL."

(3) Penn Central's announced intention to route via Maybrook traffic emanating east of Columbus, Ohio,

indicates Penn Central's self-interest in the preservation of Maybrook as a major gateway.

(4) EL has "overemphasized the effects that the NH inclusion will have upon rail competition in Southern New England" and preservation of rail competition in Southern New England is of secondary significance, particularly since the area's relatively low volume of traffic is now barely sufficient to support the operations of the NH.

(5) "The Appendix G conditions (traffic and indemnity provisions) provide sufficient protection of EL pending its inclusion in the N & W system."

(6) "Since EL's inclusion in the N & W system is now assured * * *, its ability to compete for traffic between New Haven territory and the west will be strengthened."

(7) "Affording EL the protection it now seeks might well give it and N & W superior competitive advantage."

(8) The Commission's "reserved powers are adequate to provide additional protection in the future should circumstances require it."

We agree with EL that this falls short of the meaningful analysis as to anti-competitive impact on which the Supreme Court has insisted. McLean Trucking Co. v. United States, 321 U.S. 67, 87, 64 S.Ct. 370, 88 L.Ed. 544 (1944); Schaffer Transportation Co. v. United States, 355 U.S. 83, 78 S.Ct. 173, 2 L.Ed.2d 117 (1957). As to (1), while the standard routing conditions, which have been routinely

imposed since Detroit, Toledo & Ironton Control, 275 I.C.C. 455 (1950), require that "all routes and channels of trade via existing junctions and gateways" be kept open, with neutrality of handling traffic as among connections, they do not speak to the quality of service afforded. The Commission clearly did not consider them adequate to protect CNJ, the Reading and the Western Maryland in this case and has not so considered them in many other cases EL has cited to us.[22] As to (2), while the special conditions imposed for the benefit of CNJ, Reading and Western Maryland may indeed assure against deterioration of the physical condition of the Poughkeepsie bridge route, they give no protection as to schedules affording effective connection with EL or many other factors important to maintaining service on a competitive basis. Similar considerations apply to (3); indeed they apply *a fortiori* since Penn Central is free to change its mind and would seem to have strong incentive for doing so as soon as the Selkirk facility is completed. The Commission has not shown why EL has "overemphasized" the anti-competitive effects of NH inclusion; anyway the point at issue is not competition "*in* Southern New England" but *between* New England and points to the west. The Appendix G conditions ceased to be effective on April 1, 1968, when EL was included in N & W. While inclusion in N & W will indeed strengthen EL's ability to compete by enlisting the aid of N & W solicitation and affording it one system access to many

[22] Penn Central Merger Cases, 327 I.C.C. at 563-54 (1966) [Western Maryland]; N & W Inclusion Cases, 330 I.C.C. at 867-68 (1967) [Bessemer & Lake Erie]; Western Maryland Control Case, 328 I.C.C. 684, 756-60 (1967) [N & W, Reading and CNJ]; N & W Nickel Plate Merger Case, 324 I.C.C. 1, 146 (1964) [Western Maryland].

new points, especially in the middle west, this will be of little value if Penn Central should cause the quality of the connecting service with EL at Maybrook to be downgraded in favor of New York harbor or, more particularly, after completion of the Selkirk facility, in favor of the Albany routing.

If the Commission's action is to be defended, it must thus be on the ground, numbered (7), that EL's inclusion in the N & W system, renders the present imposition of conditions similar to Appendix I inappropriate. We think it may, at least in some degree. Penn Central and N & W are now the two largest rail systems in the east, competing vigorously against each other for traffic between many hundreds of points. To require Penn Central actively to solicit traffic for N & W, see, e. g., condition 8 of Appendix I, 331 I.C.C. at 753, might rationally be deemed to go beyond what the economics of the case require or what human nature could endure. On the other hand, this reasoning would not necessarily justify the denial of conditions concerning the maintenance of train schedules, standards of service and competitive rates. And if EL has made a case for this kind of protection now, we do not consider that the extracts from the Supreme Court's decision in the Penn Central Merger Cases, 389 U.S. at 497 n. 3, 514, and 519-520, 88 S.Ct. 602, which the Commission cited in its Third Supplemental Report, would justify denial on the basis of the Commission's reserved power to attempt to undo damage that has occurred.[23]

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[23] On the other hand it would be wholly appropriate for the Commission to provide, as it did with respect to CNJ, Reading and Western Maryland, that any condition would be subject to reconsideration in the event of approval of the N & W-C & O merger.

Since the agency's opinion offers neither an analysis of the anti-competitive effect of inclusion without protective conditions or convincing evidence that pre-existing coordination with EL will be maintained, "we would shirk our duty were we summarily to approve the Commission's evaluation of the record without determining that the agency's evaluation had been made in accordance with the mandate of Congress" that the policies of the anti-trust laws be conscientiously applied. Schaffer Transportation Co. v. United States, supra, 355 U.S. at 88, 78 S.Ct. at 177. EL's request should be reconsidered by the Commission in the light of what we have said as to the inadequacy of most of the reasons advanced for the denial. Whether or not the doctrine of SEC v. Chenery Corp., 318 U.S. 80, 63 S.Ct. 454, 87 L.Ed. 626 (1943), *requires* us to remand for further consideration by the Commission rather than attempting to model conditions on our own part, it surely *permits* us to take that course.

We therefore vacate so much of the Commission's orders of November 16, 1967 and March 1, 1968, as finds the acquisition of NH by Penn Central on the terms provided in the Purchase Agreement and the interim loss-sharing and loan arrangements to be just and reasonable, and as denies EL's request for special protective traffic conditions at the Maybrook, N. Y. gateway, and remand the cause to the Commission for further proceedings consistent with this opinion. We urge the Commission and all parties to proceed with the utmost expedition. To the extent that new testimony is required, this should be held to a minimum; we do not mean by this opinion that parties who had a full opportunity to present evidence must be given

a new turn. See Jaffe, Judicial Control of Administrative Action 715 (1965). We reiterate our suggestion that the Commission make sufficiently detailed findings to avoid need for a further remand if, after the case has returned to us, the Supreme Court on appeal should disagree with any of our views. We see no need for injunctive relief at the present time.

It is so ordered.

WEINFELD, District Judge (concurring):

I concur in the remand except that as to the operating losses of New Haven I would require Penn Central to absorb these from the date of merger to the date of inclusion.

The merger was approved and found to be in the public interest only if New Haven were included—thus, its inclusion was a sine qua non of the merger. In a true sense the merger should not have been permitted absent the simultaneous inclusion of New Haven, but practical difficulties and New Haven's desperate financial plight, with the risk of irreparable injury to the public interest if the road became extinct, decreed otherwise. New Haven's critical and rapidly deteriorating situation, aggravated by the unavoidable delays inherent in reorganization proceedings, led this Court to reject the bondholders' application to stay the merger until actual inclusion. See Erie-Lackawanna R. R. v. United States, 279 F.Supp. 316, 333 et seq. (S.D.N.Y. 1967), aff'd with minor modifications, 389 U.S. 486, 88 S.Ct. 602, 19 L.Ed.2d 723 (1968). See also Oscar Gruss & Son v. United States, 261 F.Supp. 386 (S.D.N.Y. 1966), vacated and remanded on other grounds, 386 U.S. 776, 87 S.Ct. 1478, 18 L.Ed.2d 520 (1967); id., 261 F.Supp.

at 395-96 (concurring opinion). But the issue remained as to conditions to protect New Haven against continuing and increased losses during the interim period between consummation of the merger and ultimate inclusion. Its resolution was vested in the Commission.

Pennsylvania and Central, in obtaining the Commission's consent to the immediate merger without simultaneous inclusion of New Haven, agreed, absent an accord with the Trustees (subject to approval by the Reorganization Court), to abide by the terms and conditions imposed by the Commission. The Commission's order, of course, was subject to judicial review upon application by Penn Central and other interested parties.

At first the Commission directed the New Haven Trustees and Penn Central to negotiate a lease to be "immediately available upon consummation of the Penn Central merger"; however, the lawyers were of the view that the lease proposal involved too many complex problems, some of an alleged insuperable nature, to permit its consummation within time to meet New Haven's dire and worsening financial situation. Instead, the Trustees and Penn Central agreed upon, with subsequent Commission approval (with some modifications), the "loan loss" formula—a loan of $25 million by Penn Central to New Haven against Trustees' certificates over a three-year period to be charged against the ultimate purchase price for New Haven's assets with provisions whereby Penn Central, up to a limit of $5.5 million each year,[1] was to absorb 100% of the losses the first year

[1] The Commission estimated the total loss at $9.1 million but reduced the amount chargeable to Penn Central to $5.4 million by eliminating $2.6 million for rent and interest and $1.1 for retirement losses.

after the merger, 50% in the second year, and 25% in the third. Under this formula Penn Central gains the initial benefits of the merger while creditors assume year by year a larger proportion of rapidly mounting losses of operation, their application for abandonment of passenger service having been viewed as an unlikely eventuality by the Commission "in view of [its] findings * * * that the services of NH are essential."

Had that which should have been done, been done at the time of the merger, New Haven then would have become a unit of Penn Central, with the latter necessarily absorbing operating losses from the date of the merger; to require Penn Central to do so now imposes no unjust or onerous terms upon it. Penn Central, as the beneficiary of the merger, would be assuming a burden which was part of a single transaction—this, entirely apart from the creditors' claim that, constitutionally, they cannot be forced to bear the increased losses entailed by the continued operation of the New Haven pending inclusion.

I know of no businessman who would not readily absorb a unit operating at an estimated loss of $8.5 million a year (reducible by efficient operation and savings by the merged lines) as a condition of gaining potential yearly savings of $81 million—a net gain in time of $72.5 million per year which, capitalized at 8%, the rate the Commission has consistently used in this case, reflects a value in excess of $900 million—no mere bagatelle even in the instance of financial giants. Cf. Erie-Lackawanna R. R. v. United States, 279 F.Supp. 316, at 338, 342 (S.D.N.Y. 1967); Norfolk & Western R. R., 330 I.C.C. 780, at 801, 841 (1967).

In the light of the foregoing, I cannot accept that portion of the Court's opinion which, based upon a capitalization

of the estimated future loss of New Haven at $8.5 million a year after consolidation, adds $106 million to acquisition cost to Penn Central and finds the total cost to Penn Central will exceed $250 million. These losses, as noted, still leave ultimate annual savings of $72.5 million referred to in the previous paragraph.

LEVET, District Judge (concurring):

I.

I concur in the determination of the majority regarding the action of Erie Lackawanna Railroad Company.

II.

I agree with the conclusion of the majority that the remaining actions must be remanded to the Commission; however, I disagree with the reasoning of the majority upon the following matters:

(1) HARLEM RIVER AND OAK POINT FREIGHT YARDS

I agree with the majority opinion in supporting the Commission's rejection of the $32 million appraisal of Paul O'Keefe. As that opinion states, the NH Trustees submitted two reports of Arthur McCann, one at $18.1 million and one at $22.65 million (p. 433). The majority asserts, however, that the Commission's report has no adequate explanation for the rejection of the higher estimate. I see no basis for this criticism of the Commission's action.

First, the estimate of $18.1 million is based upon liquidation value which, as I understand the majority's position in "I. The Commission's Approach to Valuation of NH,"

is the accepted method. The higher valuation by McCann at $22.65 million apparently was based *not* on liquidation value but on the value to an *operating railroad.*

The Commission's report clearly indicates that it followed a net liquidation value standard (658, 659, 661) and this, as stated, is approved by the majority. NH cannot expect to receive both liquidation value and going concern value as the Commission recognized. (686-687)

(2) Real Estate Taxes

The majority opinion rules that the Commission committed error with respect to a failure to allow NH a credit of $16.2 million in real estate taxes payable by NH on transfer of assets by NH to Penn-Central free of liens. The opinion states: "We likewise see no sufficient answer to the bondholders' contention as to the failure to make a deduction for the $16.2 million of accrued real estate taxes on property required to be transferred free of liens, which, they say, resulted either in an overstatemnt of the consideration to be received by the estate or an understatement of liquidation value." (p. 438)

The majority appears to assume a balance sheet of some sort on which the assets of NH transferred to Penn-Central are computed by some basis other than net liquidation value.

This I believe is error. The standard of valuation utilized was liquidation value, and NH had real estate burdened with accrued taxes. The cost of paying taxes, concededly, is deductible in the estimate of net liquidation value. There is no basis of valuation under which some other estimate is applied.

I have not overlooked the fact that counsel for the Commission at oral argument admitted the possibility of error

on the part of the Commission. However, I believe that such statement was improvident, improperly conceded, and was, itself, an error which should not be perpetuated by subsequent findings of the Commission.

Though the position taken by the NH Trustees is not determinative, as to these items (Harlem River Yards and real estate taxes) it should be noted that the Trustees supported the Commission's original report.

(3) NH's Interest in Grand Central Terminal

I am in accord with the general conclusion that this interest must be recomputed, particularly as to NH's claim to surplus income and that the allowance to NH has been substantially underestimated.

Though the majority opinion might possibly be viewed as a determination of the relevant legal issues, and although I have the highest respect for my colleagues, I am unable to join in the entire legal conclusions reached for the following reasons:

(a) It does not appear that all facts of a long record of some sort of a joint effort of NH and New York Central at Grand Central Terminal were submitted;

(b) No agreement on such facts by NH and by Penn-Central is revealed;

(c) No plenary adversarial judicial proceeding has taken place;

(d) I entertain substantial doubts of the jurisdiction of this court to make any legal disposition of such issues. I am unable to discern clear-cut findings of fact, conclu-

sions of law, or the equivalent relative to NH's interest—except that the majority states: "We conclude by the same token that NH's claims to share in surplus income over and above all terminal expenses are exceedingly strong." (p. 431) "• • • All told it would be fair to assume that these readjustments will increase the liquidation value of NH's interest in the GCT properties to at least $25 million." (p. 432);

(e) The Commission has neither the authority nor the expertise to determine the complex legal issues which govern the extent of NH's interest in Grand Central Terminal, and, hence, the Commission has no inherent present ability to determine what valuations are fair or proper.

In short, to send this maze of intricate legal perplexities, which include complex accounting and valuation problems, as one unit back to the Commission is futile, and any future ruling by the Commission can be little more than a mere guess based upon uncertainties.

It is my belief that practicality demands a different approach. I suggest the present elimination of any allowance to NH for Grand Central Terminal and a deferral or reservation of any adjustment therefor until the questions have been finally determined by a court of competent jurisdiction, and the Commission, with full knowledge of such determinations, has made a considered and a complete valuation.

I see no reason why this is not proper and practical, and any other procedure will surely create further dispute and futile litigation. The parties might well stipulate to this procedure upon such terms as would impose no unfairness because of such partial deferment.

(4) Cost of Acquisition of NH to Penn-Central

I do not disagree with any portion of the majority opinion as to cost of acquisition. I do, however, feel compelled to note that I believe consideration of this feature to be unnecessary under the theory adopted by the Commission.

CONCLUSION

Despite the objections stated, I agree that this entire matter must, nevertheless, be remanded to the Commission for the other reasons stated by the majority.

Memorandum Opinion of the Three-Judge Court on Penn Central's Motion for Reargument

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THE NEW YORK, NEW HAVEN and HARTFORD RAILROAD COMPANY, FIRST MORTGAGE 4% BONDHOLDERS COMMITTEE, *et al.*,

Plaintiffs,

v.

UNITED STATES OF AMERICA and INTERSTATE COMMERCE COMMISSION,

Defendants.

UNITED STATES DISTRICT COURT

S. D. NEW YORK

68 CIV. 296, 306, 308, 344, 345

CONSOLIDATED ACTIONS

MEMORANDUM

Intervening defendant Penn Central Company has moved for reargument of two issues determined or discussed in the opinions filed July 10, 1968.

I.

The first is our statement, p. 18:

> "... we see no basis for determining the NH's share of the surplus income on the ground of car-use; when NH participated in building construction, it did so as an equal and should share on that basis."

Penn Central claims that this gave insufficient weight to the car-use formula established by § 4 of the 1907 agreement

and that, at the very least, the Commission's use of a 40% figure for determining NH's share in the surplus income, 331 I.C.C. at 684, was not irrational. Inconsistently with the latter position, Penn Central also argues that "since the New Haven's maximum share of excess income is its car-use percentage, and since on cessation of car entrances its car-use percentage would be zero, under the liquidation hypothesis which underlies the liquidation value studies, the New Haven's claimed share of excess must also be zero."

Judges Friendly and Weinfeld find the argument altogether unpersuasive. Car-use was a formula, and a wholly appropriate one, for sharing expenses. So long as income from the Terminal and its properties did not exceed expenses, the effect of § 14, dedicating the income to the payment of terminal expenses, was indeed that each company would benefit from such income in proportion to its car use. But nothing in either the 1907 or the 1913 agreement suggests car-use as an appropriate basis for apportioning the then unexpected surplus income. When the companies agreed in 1913 that NH should have a right to "join" with the central "in the construction, holding, maintenance and leaving of buildings" they must be taken to have meant that NH could join as an equal, subject only to the dedication of the income to terminal expenses. The Commission gave no reason for using a car-use formula in determining NH's share of surplus income, but simply adopted a claim by the NH Trustees which we regard as unduly favorable to the Central. In any event the construction of contracts of this sort is not the kind of matter where a court need bow to administrative expertise. See NLRB v. Marcus Trucking Co., 286 F.2d 583, 591 (2 Cir. 1961).

Judge Levet adheres to the views with respect to the Grand Central Terminal properties expressed in his opinion.

II.

Penn Central's second point relates to our requiring, pp. 20-21, the Commission adequately to explain its acceptance of the lower of two appraisals of the Harlem River and Oak Point Yards made by Mr. McCann for the NH Trustees, 331 I.C.C. at 668. It argues that we erred in thinking the $4.55 million difference between McCann's two appraisals represented an allowance for expenses and discount to present value which may have been duplicated elsewhere, and contends the true explanation for the difference was that the higher appraisal assumed continuation of some railroad operations whereas the lower did not. However, Judges Friendly and Weinfeld see nothing to be gained by our now attempting to decide this. The Commission is entirely free to consider Penn Central's contentions, as well as a suggestion made to us at the argument, that the assumption of complete lack of railroad facilities failed to take account of the proximity of a line of Penn Central; it should also explain its rejection of Mr. O'Keefe's industrial appraisal. We require only a reasoned explanation of whatever figure the Commission, on further consideration, finds to be proper.

Judge Levet adheres to the view that no remand on this issue should have been required.

The motion for reargument is denied. So ordered.

HENRY J. FRIENDLY
U.S.D.J.

EDWARD WEINFELD
U.S.D.J.

RICHARD M. LEVET
U.S.D.J.

August 5, 1968.

Opinion of the Three-Judge Court on Penn Central's Application to Stay Inclusion

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PENN CENTRAL COMPANY,

Plaintiff,

—against—

UNITED STATES OF AMERICA,
INTERSTATE COMMERCE COMMISSION, *et al.*,

Defendants.

UNITED STATES DISTRICT COURT
S. D. NEW YORK
68 Civ. 5121

December 27, 1968.

Before FRIENDLY, Circuit Judge, and WEINFELD and LEVET, District Judges.

• • •

Judge Friendly: Gentlemen, in view of the exigencies of time and of the possibility that it may be desired to take this matter elsewhere before January 1, we have determined to follow the English practice and deliver our judgment forthwith. We are able to do that because we have had the benefit of the excellent brief of Penn Central and of the Commission's report and Judge Anderson's order and memorandum for several days and therefore were able to narrow what we needed to gain by the oral argument.

And the issue raised by Penn Central's application for a temporary injunction is a narrow one. Summarily stated,

it is as follows: Under condition No. 8 of Appendix A to the Commission's approval of the merger of the Penn and the New York Central, reported in 327 ICC 475 at 553, which was carried forward into the Commission's final order of June 9, 1967, can the Commission lawfully direct the actual inclusion of the New Haven in Penn Central when the Commission has once fixed fair and equitable terms, those have been reviewed by the reorganization court and by this court, and found wanting in certain respects, the Commission has then fixed new, fair and equitable terms on remand but there has not yet been an opportunity for the parties to obtain a further round of judicial review?

By order dated December 24, 1968 the reorganization court has directed the trustees of New Haven to transfer the properties specified in its order at 11:59 p.m. on December 31, 1968 and Penn Central to make the payment of $145.6 million in cash, bonds, stock and otherwise as described in the Commission's order of December 2nd, reported at 334 ICC 25 at 71.

The order of the reorganization court states in paragraph J, "The conveyance of the debtor's assets by the New Haven trustees and the payment of consideration by Penn Central Company as provided herein shall be without prejudice to the right of any party to contest the fairness and adequacy of the consideration and the other terms of the inclusion of the debtor's operation in Penn Central Company."

We understand that to be a two-way street.

We pause at this point to note the issue to which Mr. Auerbach directed a considerable portion of his argument, and we do agree that it would be inappropriate for us even to consider an injunction against this order of the reorganization court. If Penn Central desires to be relieved of any directions made to it in that order, its remedy must lie

in further application to that court or in the Court of Appeals.

Its request for an injunction from us is necessarily limited, as Mr. Perkins indicated, to the compulsion contained in the order of the Commission, which, as the context of the report at pages 47 and 76 makes sufficiently clear to us, was intended at least to permit what the reorganization court has done. What course Penn Central would have to follow with respect to the order of the reorganization court if an injunction against the Commission's order were to be granted would be a problem for its counsel, with which we are not concerned.

The Commission's direction of inclusion prior to opportunity for judicial review of the terms which it had fixed on remand stems from a stern reality. This was the opinion of August 15, 1968, in which the reorganization court concluded that any further absorption of losses after December 31 would constitute a taking of the New Haven's property without due process of law, modified a previous order so as to withdraw the authority of the New Haven trustees to make borrowings from Penn Central after January 1, 1969 which admittedly are needed to keep the railroad in operation, and declared that absent actual inclusion prior to January 1, 1969 "the trains will stop."

While Penn Central suggests that less draconian options were open to the reorganization court and still may be, that court has recently reaffirmed its position. The Commission lacked power to alter this, and so do we.

Condition No. 8 of the order approving the Penn Central merger was imposed pursuant to Section 5(2)(d) of the Interstate Commerce Act, which provides:

"The Commission shall have authority in the case of a proposed transaction under this paragraph involving a rail-

road or railroads as a prerequisite to its approval of the proposed transaction to require upon equitable terms the inclusion of another railroad or other railroads in the territory involved upon petition by such railroad or railroads requesting such inclusion and upon a finding that such inclusion is consistent with the public interest."

Penn Central contends that this demands that the equitable terms should have been established beyond any possibility of change as a result of judicial review before inclusion can be directed. So broadly stated, the argument is not sustainable. The language of Section 5(2)(b) dealing with voluntary proposals on which Penn Central relies is of little aid with respect to the entirely different problem under Section 5(2)(d). When a merger is proposed under 5(2)(b), the authorities will have worked out the terms, the Commission must determine whether these are just and reasonable, and its order is permissive only.

When a railroad not a party to such a merger requests inclusion, the terms will often, indeed, perhaps usually, not have been agreed. In such cases, the Commission, if it finds inclusion to be required, authorizes the merger subject to the agreement, manifested by consummation of the merger, to include the non-party in such language as "under such terms as may be found equitable to all parties involved"—that was the language used in the Norfolk & Western merger—or as here, ". . . upon such fair and equitable terms as the parties may agree subject to the approval of the Bankruptcy Court and the Commission . . . in the event the parties are unable to reach an agreement (and subject to approval by the Bankruptcy Court) such inclusion shall be upon such fair and equitable terms and conditions as the Commission may impose."

We have heard no suggestion that this procedure does not comply with the Act, even though at the time of the authorization of the principal merger the Commission obviously cannot know what the precise financial consequences to the merged company from the enforced takeover of a non-party will be.

Where the matter is left thus open-ended, the parties to the merger are, of course, entirely free, if they wish, to refrain from consummating it until the blanks in the check are filled. On the other hand, as stated clearly in the Penn Central order, "Consummation of the merger by the applicants shall indicate their full and complete assent to these requirements."

It seems to us that no argument is really needed to show that the language of the Penn Central merger order which we have just quoted literally covers what the Commission has here directed. Inclusion of the New Haven was required "upon such fair and equitable terms as the Commission may impose." We have no such situation in Schwabacker against United States, 334 US 182, where the Commission had turned over to a state court part of the job Congress had directed it to perform. The Commission here has done all that it can do. The question is whether we should superimpose upon the literal meaning of the Penn Central merger order a gloss that an actual takeover of the New Haven cannot be directed until the process of judicial review and possible further remand has come to an end.

In the usual case, where the railroad seeking inclusion is a going concern, this problem will scarcely arise, since the road seeking inclusion will wish to know the final terms before seeking stockholder approval. If it were to arise, any argument against inclusion would have scant appeal.

If the courts found occasion to upset the Commission's conclusions as to what were equitable terms, the Commission would simply be required to modify the terms it had first set and prescribed others that would satisfy the decree of remand, and there would be no reason to anticipate difficulty in its doing so.

The special problem here arises from the insistence of the New Haven bondholders that they are constitutionally entitled to the liquidation value of the New Haven as of December 31, 1966. Although one might suppose that a price to which the New Haven is constitutionally entitled, if it were so held, could not be inequitable, Penn Central argues to the contrary. It says that because of the different considerations involved there is a possibility that if the courts should sustain the bondholders the lowest price equitable to the New Haven might be higher than the highest price equitable to Penn Central, the Commission might therefore feel required to refuse to up the price to the figure set for the New Haven, and the inclusion would have to be unscrambled, yet that would be quite impracticable.

We do not quarrel unduly with the proposition that unscrambling would be exceedingly difficult. While we also concede some theoretical merit to the other propositions, we regard the argument as lacking in reality, or, in the Commission's language, as based on "exaggerated fears."

The Commission has found a net liquidation value of the New Haven as of December 31, 1966 of $162.7 million as against a fair price of $140.6 million plus $5 million of 1968 operating losses.

While the bondholders may attack the former figure as inadequate, and we in no way prejudge such claim, our study of the report on remand indicates a thorough and conscientious effort by the Commission to follow the direc-

tions with respect to the determination of liquidation value made by the reorganization court and ourselves.

And even if we or the reorganization court should reject both of the Commission's downward adjustments, one of $15.4 million for an additional year's delay in starting the liquidation and the other of $6.7 million for a bulk sale discount, which we, of course, in no way suggest, and if we should be sustained by the Supreme Court in doing so, the excess above the price the Commission has found fair and equitable would not be such as to create, in our view, any real chance that in a transaction of such magnitude and public consequence the Commission would conclude that the camel's back had been broken.

Perhaps, indeed, it is not too much to hope that with the area of true controversy narrowed as we think it now has been, the parties may be able to compromise their differences and bring this long litigation to an end.

The only other point raised by Penn Central requiring discussion is its fear that under the decision in St. Joe Paper Company against Atlantic Coast Line, 347 US 298, the reorganization court may have lacked power to direct the conveyance. Assuming that this issue is properly before us, we think a sufficient answer lies in the lack of objection by any security holder to the order of the Bankruptcy Court.

Weighing, therefore, what we regard as the small possibility of injury to Penn Central from a denial of a temporary injunction against the irreparable injury to the public which has been stated by Judge Anderson and really not disputed by anyone from a granting of the injunction, we deny the motion for a temporary injunction in the exercise of our discretion.

If the clerk will give me the original of the motion papers, we will endorse that.

Opinion of the Three-Judge Court Dismissing the Complaint of the Providence & Worcester R.R. Co.

MANUFACTURERS HANOVER TRUST CO., *et al.*,

Plaintiffs,

v.

UNITED STATES of America and Interstate Commerce Commission,

Defendants,

No. 68 Civ. 5200.

United States District Court

S. D. New York.

April 28, 1969.

Before FRIENDLY, Circuit Judge, and WEINFELD and LEVET, District Judges.

FRIENDLY, Circuit Judge:

These consolidated actions raise a host of difficult and important questions concerning the Fourth Supplemental Report of the Interstate Commerce Commission in the Penn Central merger case, 334 I.C.C. 25 (1968). This report, like its two predecessors, deals with the inclusion of the New Haven (NH). We deal in this opinion only with a small and discrete segment relating to intervening plaintiff Providence & Worcester R. R. Co. (P & W), which we have singled out for advance disposition because the Commission's report and order allow Penn Central (PC) to terminate the lease of P & W unless by June 30, 1969

that company takes certain action to which it objects.

The main line of P & W extends, as its name implies, from Providence, R. I., where it joins with what were the lines of NH and the Boston & Providence, to Worcester, Mass., where it connects with the former Boston & Albany. Currently it is only a freight line. On July 1, 1892, P & W leased all its property to NH for 99 years. NH was to pay an annual dividend of $2.50 per share on P & W's stock, interest on its bonds, and all taxes. At the time of the Commission's report NH owned 28% of the P & W stock and these shares have now passed to PC. The NH trustees rejected the P & W lease by an amendment to their plan of reorganization, and the Commission's order confirms this rejection.

P & W petitioned the Commission for inclusion in PC as a leased line under the terms and conditions of its lease with NH. The I.C.C. did not pass on this in its earlier reports, but PC does not dispute that the condition with respect to inclusion of NH in the merged company, 327 I.C.C. 475, 526-27 (1966), entitled the Commission now to require inclusion of P & W. In the report here under review, the Commission directed such inclusion as in the public interest, 334 I.C.C. at 89-90, and found that the present lease constituted equitable terms, with two exceptions. One, not here contested, is that, although the lease extends until June 30, 1991 PC may terminate it at an earlier date if the Commission grants permission to abandon under § 1(18) of the Interstate Commerce Act. The other relates to provisions in the Massachusetts and Rhode Island charters of P & W. The company was incorporated in both states, and both charters provided that every stockholder had one vote for each of the first 50

shares he owned but only one vote for every 20 shares after that, and that no single stockholder could have more than a quarter of the voting power. The result would be that PC's 9551 P & W shares, 28% of the total shares, could cast only 485 votes, 3% of the total votes. Sustaining PC's objection to these restrictions, the Commission directed that unless they were eliminated in favor of "a one-share one-vote provision" by June 30, 1969, PC might terminate the lease on notice to P & W's board of directors and the Commission and P & W would thereafter be operated by PC, without a lease, for P & W's account.

P & W's first objection to this direction was that the legislatures of Massachusetts and Rhode Island must approve any charter amendments, and that it would be impossible to obtain the necessary legislation in the time allowed. However, as P & W now recognizes, any difficulty on this score has been overcome by the Commission's granting P & W's request to merge, on a share for share basis, with the Providence & Worcester Co., a Delaware corporation, F.D. No. 25357, served February 18, 1969. Although the certificate of incorporation of the Delaware company preserves the voting restrictions of the Massachusetts and Rhode Island charters, these can be altered through amendment by a majority vote of stockholders without any need for legislation.

P & W's other objections, that the Commission lacked power to impose the condition since this was unrelated to transportation and that the Commission's action was unwarranted, are best considered together. The I.C.C. took note of PC's position that the voting provisions would prevent PC's including P & W's operations in a consolidated tax return unless it were able to acquire 100% of the

stock and would enable a relatively few stockholders to veto any attempt at simplification of PC's corporate structure by acquiring P & W through merger or purchase. Such considerations are sufficiently related to transportation to come within the Commission's broad power to condition P & W's inclusion "upon equitable terms," § 5(2) (d). While their force is not overpowering, neither was that of P & W's objections, namely, that "one share, one vote" would prejudice the public stockholders if PC presses an abandonment application or diverts traffic in an effort to improve its case for this. PC cannot obtain abandonment by securing the consent of P & W as a corporation. Affected shippers and communities and the public stockholders will be entitled to be heard, and all figures relating to P & W's operations will be subject to expert scrutiny. Also we do not read the Commission's report as preventing provision for cumulative voting. The balancing of these considerations was for the Commission.

There is equally little force in P & W's contention that the Commission could not provide that in the event of its refusal to change the voting provisions and consequent termination of the lease, PC should operate the road for the lessor's account. Despite termination of the lease PC would still be bound to operate P & W until granted authority to abandon. Either it or P & W can apply for this, and the I.C.C. can fix the fair rent for the interim. Thompson v. Texas Mexican Ry., 328 U.S. 134, 144-145, 146-150, 66 S.Ct. 937, 90 L.Ed. 1132 (1946). We perceive no reason why operation for the lessor's account after termination of the lease would be inappropriate; the Commission doubtless drew on the analogy of § 77, c(6) of the Bankruptcy Act.

This leaves one other matter. One of PC's objections to P & W's insistence that PC operate under the terms of the lease related to various claims against NH which P & W had asserted thereunder. In overruling this, the I.C.C. said "Such disputes and claims will become the responsibility of Penn Central whether or not it becomes the lessee of P & W." 334 I.C.C. at 89. PC's opening brief in this court complained of this statement if it meant to refer to "pre-inclusion claims" which, PC asserted, were the responsibility of the NH estate. The brief for the United States and the Commission agreed that it would be inequitable to burden PC with in personam claims that had accrued against the NH estate, with the result of preferring P & W over other NH creditors, or with claims against moneys in the hands of the NH trustees representing sales of P & W property. The brief read the quoted language as preserving against PC only such claims of P & W as would be good against a purchaser of the leasehold and thus were PC's "responsibility" at least in the first instance, notably, pre-inclusion claims that various parcels of real property should be conveyed to P & W. Concerning these, the brief suggested that the reorganization court reserve jurisdiction over PC's asserted entitlement to a refund if conveyances were required. The Commission had made a similar statement with respect to the claims to be assumed by PC in its report approving the merger of P & W and the new Delaware company. PC is content with the condition as so interpreted but P & W argues that counsel cannot alter the Commission's order. While the I.C.C.'s method of expression left something to be desired, the construction put upon it by government counsel accords with good sense and equity whereas P & W's does not, and jibes

also with what the Commission itself has later said. No purpose would be served by our remanding to enable the Commission to amend the earlier report to accord with the later one, as we are sure it would.

The complaint of P & W as intervening plaintiff is accordingly dismissed for failure to state a claim on which relief can be granted. There being no just reason for delay, we hereby direct the entry of a final judgment to that effect, F.R.Civ.P. 54(b).

Opinion of the Three-Judge Court Relating to the I.C.C.'s Fourth Supplemental Report

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THE NEW YORK, NEW HAVEN AND HARTFORD RAILROAD COMPANY, FIRST MORTGAGE 4% BONDHOLDERS' COMMITTEE, THE CHASE MANHATTAN BANK, N.A., as Trustee Under the General Income Mortgage of the New York, New Haven and Hartford Railroad Company, MANUFACTURERS HANOVER TRUST COMPANY, as Trustee of the First and Refunding Mortgage of the New York, New Haven and Hartford Railroad Company, and OSCAR GRUSS & SON,

Plaintiffs,

v.

UNITED STATES OF AMERICA and INTERSTATE COMMERCE COMMISSION,

Defendants,

PENN CENTRAL COMPANY, STATE OF NEW YORK, and STATE OF CONNECTICUT,

Intervening Defendants.

UNITED STATES DISTRICT COURT
S. D. NEW YORK
Nos. 68 CIV. 5200, 5210,
69 CIV. 11, 12

Before FRIENDLY, Circuit Judge, and WEINFELD and LEVET, District Judges.

FRIENDLY, Circuit Judge:

On July 10, 1968, this court vacated "so much of the Commission's orders of November 16, 1967 and March 1, 1968, as finds the acquisition of NH by Penn Central on the terms provided in the Purchase Agreement and the

interim loss-sharing and loan arrangements to be just and reasonable" and remanded the cause to the Commission for further consistent proceedings. 289 F.Supp. 418, 448. We urged the Commission and all parties "to proceed with the utmost expedition" and to hold new testimony to a minimum. By order dated August 13, 1968, Judge Anderson, in the District Court for Connecticut, presiding over NH's reorganization under §77 of the Bankruptcy Act, made an order similar in tenor. 289 F.Supp. 451. The reorganization court added one highly significant further item—a direction that unless the Commission issued an order requiring Penn Central (PC) "physically to take over and commence operating the New Haven Railroad, not later than January 1, 1969, leaving the price and the other terms of the inclusion to be determined later," that court would consider itself "forced to entertain a motion to dismiss the reorganization proceedings" and "while liquidation will have to await authority to abandon, the trains will stop in January . . . ." 289 F.Supp. at 459. The Commission acted with expedition, rendering its Fourth Supplemental Report (the Remand Report), on December 2, 1968. 334 I.C.C. 25. In response to Judge Anderson's opinion, it ordered PC to take over operation of NH at midnight on December 31, 1968, and to pay the price fixed by the Commission, which would, however, be subject to judicial review. 334 I.C.C. at 74-78. The reorganization court approved this order on December 24, 1968; we denied PC's application to enjoin its execution; and the take-over was effected as scheduled.

On the other hand, our hope that the proceedings on remand would be of limited scope has not been realized. Both sides introduced much new evidence on subjects we

had not expressly included in our remand, the Remand Report contains much new analysis, and we are confronted with almost as many issues as when the case was previously before us. We intend no criticism of the Commission on this score. While an administrative agency may choose to confine itself to the precise issues remanded, it is not bound to do so but may receive and consider such further evidence as it thinks requisite or desirable for the proper discharge of its duties. See FCC v. Pottsville Broadcasting Co., 309 U.S. 134, 145 (1940); Fly v. Heitmeyer, 309 U.S. 146, 148 (1940). Moreover, with particular respect to the two large downward adjustments made under the heading "Other Pricing Considerations," 334 I.C.C. at 53-63, we see no reason for refusing to accept the Commission's explanation, 334 I.C.C. at 54:

> In the *inclusion* report, we found that the consideration Penn Central had agreed to pay would equal liquidation value there shown, and that made it unnecessary for us to explore other pricing considerations. The liquidation value that results in this reopened proceeding exceeds the agreed price, obliging us to make a new determination as to whether the price resulting from such a valuation is fair.

Broadly speaking, what the Commission did in the Remand Report was this:

On reexamination it found that if liquidation of NH would have been completed by selling off the properties individually in a normal market within six years from the date when a determination to liquidate had been made, the estate would have realized a figure having a present worth of $162.7 million. 334 I.C.C. at 30-53. It next argued

that it was not constitutionally required to allow NH this or any other estimate of liquidation value, but only "a fair and equitable price under Section 5 of the Interstate Commerce Act," 334 I.C.C. at 56. However, it found no need to base its decision on this ground, since it also found that

> The alleged right to liquidation values derives from an alleged right to abandon; and there are recognized limitations on the right to abandon that in themselves limit the creditors' entitlement to the liquidation value we have computed under the court's instructions. 334 I.C.C. at 57.

By making two further adjustments to liquidation value, the Commission reached a figure which it considered "a fair price on the current record," and it is this sum which is before us for review.

The two adjustments were of $15.386 million for a one-year delay before the start of liquidation due to the need for obtaining a certificate of abandonment, 334 I.C.C. at 58-60,[1] and of $6.695 million for the lesser amount that would be realized if the properties were sold at one time as a unit rather than piecemeal over a six-year period, 334 I.C.C. at 60-63. These reductions, aggregating $22.081 million, led to a fair purchase price of $140.6 million, to which the Commission added $5 million as PC's equitable share of NH's losses from February 1, 1968 (the date of

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[1] This consisted of three items:

	Millions
Year's added discount	$ 7.946
Year's preservation costs	4.940
Year's real estate taxes	2.500
	$ 15.386

the PC merger) to December 31, 1968, 334 I.C.C. 65-71. The parties are in disagreement not only with respect to the propriety of the two large deductions but also concerning countless items of liquidation value and of consideration. We shall not attempt to canvass all these points but will deal with such, quite sufficient in number, as we deem to merit discussion.

I. *The Scope of Review and the Governing Standard*

We begin by reiterating the severe limitations on the scope of our review. In our last opinion in this case, 289 F.Supp. at 427, we called attention to what we had said on that subject in the N & W Inclusion case, 279 F.Supp. 316, 337 (1967), aff'd with minor modifications, 389 U.S. 486 (1968). We also cited Mr. Justice Cardozo's pertinent admonition, "An intelligent estimate of probable future values, . . . and even indeed of present ones, is at best an approximation. There is left in every case a reasonable margin of fluctuation and uncertainty." Dayton Power & Light Co. v. Public Utility Comm'n, 292 U.S. 290, 310 (1934).[2] Such considerations are peculiarly applicable to a determination so hypothetical as the liquidation value of the New Haven. What that really is, no one ever has known or ever will know, even approximately. The idea of the states of Connecticut and Rhode Island and of a large part of Massachusetts being without rail service is so unthink-

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[2] The Commission observed in the Remand Report:

> "Valuation is at best imprecise, involving broad areas of judgment. This is especially so in the case of a bankrupt railroad having no prospect of future income as it is presently operated." 334 I.C.C. at 54.

able that its consequences on land values are beyond possibility of accurate calculation. When passing on such an issue, it is peculiarly important for a reviewing court to remember that its function is only to make certain that agency actions "are based upon substantial evidence and to guard against the possibility of gross error or unfairness." Penn Central Merger and N & W Inclusion Cases, 389 U.S. 486, 524 (1968).

When the case was last before us, we noted various faults and fuzzy patches in the Inclusion Report, but the principal ones were what amounted to two arithmetical errors aggregating more than $20 million, 289 F.Supp. at 427-28, 438, and a substantial understatement, stemming from a plain misconception on a matter of law, of the value of NH's claim to half of the "excess income" from the Grand Central Terminal properties, 289 F.Supp. at 428-30. The arithmetical mistakes could have been corrected without a remand, and it might also have been possible to make our own determination with respect to the GCT properties. However, since the Commission had justified its approval of the price fixed in the Purchase Agreement on the basis that it reflected the liquidation value standard for which the NH bondholders were contending, without, however, committing itself to the need for going so high, and we found this factual position was not borne out by the record, we remanded in order to give the agency an opportunity either to revise its results in the light of our finding or, if so advised, to explain why no revision was required. 289 F.Supp. 440-41. We also thought it best that the Commission should undertake the complex task of setting a value on the GCT properties under the legal standards we had laid down with respect to the strength of

NH's claims, and, since there was to be a remand in any event, that it should explain certain other obscurities.

On this second review we confront once more the question of the proper standard of valuation, which has now been fully discussed by the Commission. 334 I.C.C. 53-57. This matter apart, no significant appeal is made to our authority to interpret the Constitution, statutes, or contracts. There are again a few alleged arithmetical errors, this time relatively minor. But the overwhelming bulk of the attacks concerns the Commission's economic judgments. With respect to these we must be on guard lest the familiarity about the facts of the case we have somewhat painfully gained should lead us simply to substitute our views for those of the agency which Congress has appointed.

We begin with a word on whether the Commission was bound to award liquidation value although, like the Commission, we do not find it necessary to decide this. One can scarcely quarrel with the proposition that in general "A fair and equitable price . . . means a price that is fair both to the buyer and to the seller." 334 I.C.C. at 56. In the Norfolk & Western Inclusion Case, 330 I.C.C. 780, 801 (1967), the first instance in which the Commission was required to prescribe a price, it said:

> In the ordinary case under section 5(2)(d) the acquired line's maximum commercial value to the acquiring line cannot exceed a price based upon past and foreseeable earnings of the acquired line plus the value of all benefits the acquired line brings to the acquiring line's system. Moreover, this price is ordinarily the maximum we should expect the acquiring line to pay. It appears that the price, nevertheless,

will generally be below book value, and hence it will ordinarily be the minimum price the acquired line will find tolerable.

The prices the Commission set on this basis were later upheld by the Supreme Court, Penn Central and N & W Inclusion Cases, 389 U.S. 486, 524 (1968), not simply as against the acquiring line's contention that they were too high but as against a claim by one of the lines to be acquired that the price, considerably less than current market quotations, was too low.

Here the "past and foreseeable earnings of the acquired line" are huge and increasing deficits—deficits far larger than in 1966 when the Commission required inclusion of NH as a condition of the Penn Central merger, 327 I.C.C. 475, 526-27 (1956). The only "benefit" inclusion of NH is claimed to bring to PC is that the Commission would not have approved the Penn Central merger without it. The Commission has rejected the arguments of the NH bondholders based on adding to the value of NH whatever potential savings from the merger are needed to justify a high inclusion price, saying, "This was not the intent of our decision," 334 I.C.C. at 66, a view we had previously intimated, 289 F.Supp. at 443. There is thus a decided anomaly in the position that, looking only at the words of the statute, the Commission was required to make PC pay a price for NH which is far beyond anything NH is worth to it in an economic sense and which, by hypothesis, it can never realize.

A more difficult question is whether the Fifth Amendment for bids application of the statute in such a manner as to produce a price less than liquidation value on the facts here presented. When the case was last before us,

we indicated tentative agreement with that position. We cited authorities which established in our view that a railroad with no reasonable hope of future earnings, such as NH, had a "constitutional right . . . to cease operations and liquidate," 289 F.Supp. 440, since to force operation at a loss "would be to take its property without the just compensation which is a part of due process of law." Railroad Commission v. Eastern Texas R.R., 264 U.S. 79, 85 (1924); Bullock v. State of Florida ex rel. Railroad Commission, 254 U.S. 513 (1921); Brooks-Scanlon Co. v. Railroad Commission, 251 U.S. 396 (1920). Despite observations in the Commission's report, 334 I.C.C. at 55-57, we adhere to that view, for reasons fully developed in the recent opinion of the reorganization court, subject only to the qualification that liquidation of NH could not commence until the Commission, acting with appropriate speed under § 1(18) of the Interstate Commerce Act, had issued the certificate of abandonment to which NH would have been constitutionally entitled. We believe this position is also supported by two opinions of Mr. Justice Brandeis which we read as declaring that while Congress may in the public interest subject a secured creditor to reasonable delays in realizing on his security, it may not deprive him altogether of his right to sell the *res* at public auction. Louisville Joint Stock Bank v. Radford, 295 U.S. 555 (1935); Wright v. Mountain Trust Bank, 300 U.S. 440 (1937).

However, we are not so sure now as we formerly were that these precedents necessarily lead to the further conclusion concerning the Commission's duty here that the NH bondholders would draw from them. The just compensation and due process clauses are triggered only by governmental action. Existence of governmental compulsion was not dis-

puted in any of the cases cited above; it is disputed here, for PC argues that although the bondholders seek compensation for governmental taking of a right to liquidate, they never properly asserted such a right. The NH trustees petitioned for inclusion in PC about three months after the merger application was filed in 1962. The bondholders at first supported this move, and it was not until April 1967, long after the commitment to seeking inclusion was for practical purposes irrevocable, that some of them petitioned to dismiss the reorganization. Judge Anderson denied this, 281 F.Supp. 65 (1968), the decision was not appealed, and when immediate inclusion was finally ordered, it was without protest from any party except PC. If we could take all this as indicating that inclusion had in fact been sought solely because the bondholders and the trustees felt it would be more in NH's interest than abandonment, we would find nothing in § 5(2)(d) or in the Fifth Amendment that would prevent the Commission's fixing a price considerably short of liquidation value and saying, in effect, "This is all we think it fair for the acquiring road to be required to pay. We see no reason why it should be made to assume the entire cost of keeping alive a carrier whose operations the public will not support. On the other hand, if you [the seller] don't like it, you are free to refuse and seek the abandonment to which you are entitled."

On the other hand, the present case may well be one where a volume of history must prevail over a page of logic. Ever since June 1962, when the Trustees petitioned for inclusion of NH if the PC merger was approved, it so vastly preferable in the public interest that, as we thought, 289 F.Supp. at 444, and the Commission now has has become increasingly apparent that this solution was

confirmed, 334 I.C.C. at 59, "If the Trustees had presented abandonment applications as an alternative to sale, the Commission would almost certainly have deferred their consideration for a reasonable period while inclusion was being explored." The bondholders say, with considerable force, that this known attitude of the Commission was the practical equivalent of the denial of an application for abandonment and entailed an obligation to procure for them what they could have realized on abandonment if inclusion became a reality. They point out also that, during the long period when the PC merger was pending and before inclusion occurred, they have been making a substantial contribution to the public interest through the erosion of their property by losses of cash after any real possibility of a viable service had disappeared. Hence, the proper administration of § 5(2)(d) may require at least a close approach to what they could have realized in an assumed liquidation even though, because of the absence of an actual taking or other governmental compulsion, the Fifth Amendment does not.

Because of the way the Commission has approached the valuation question, we do not feel called upon finally to decide these intriguing issues. The Commission set out to fix a price that would give NH what it thought the estate could realistically hope to achieve on liquidation. If the Commission made demonstrable errors, it is our duty to correct these, hopefully without a still further remand. But, as indicated, we are not required, or indeed permitted, to reexamine every judgment made by the Commission and to substitute our own whenever we think it better. Our function is to determine whether the agency's conclusions are "equitable and rational," not "to second-guess each step

in the Commission's progress of deliberation." Penn Central Merger and N & W Inclusion Cases, 289 U.S. 486, 524 (1968).

II. *The One-Year Delay for an Abandonment Proceeding*

At the initial hearings concerning inclusion, the NH trustees submitted estimates of asset values as of the end of 1965, and PC submitted estimates as of the end of 1966. In the Inclusion Report, the Commission by and large accepted the former figures, then adjusted them to the later date, spread them over a six-year estimated liquidation period, and discounted them back to present value. At that stage the Commission was thus assuming a liquidation starting January 1, 1967. The further adjustment in the Remand Report amounts to assuming that the decision to liquidate would have been taken on that date but that liquidation could not begin until a year later because of the necessity for obtaining a certificate of abandonment under § 1(18). Passing on the reasonableness of such a determination requires a reviewing court to enter a never-never land. The Commission had to estimate the starting date of a liquidation that never happened, that in the world as we know it scarcely could have happened, and that, if it had happened, could have happened in any one of a number of equally imaginary ways, each based on a different pattern of demands on governmental authority that were never made, and ensuing administrative and judicial proceedings that never occurred.

We find no lack of rationality in the Commission's view that even if the liquidation decision is assumed to have been taken by the end of 1966, although in fact the bond-

holders did not apply for dismissal of the reorganization proceedings until the spring of 1967, authority to abandon would not have been granted until a year thereafter, even though we believe, as the Commission may not, that it would have been constitutionally required to issue a certificate of abandonment if inclusion was not a viable alternative. Even in such a case an abandonment proceeding serves the important office of affording persons interested in maintaining the service, here the four states directly concerned, an opportunity to make proposals for acquiring so much of the property as was considered essential. See Palmer v. Massachusetts, 308 U.S. 79 (1939); Meyer v. Jay St. Connecting R.R., 259 F.2d 532 (3 Cir. 1958). The NH bondholders answer that except for the probability of inclusion in PC they would have insisted on abandonment at a much earlier date and that the states have already had such abundant opportunity to make proposals to take over NH's operations that no significant further period could properly have been accorded. Despite the forceful exposition of these arguments in the recent opinion of the reorganization court and in Judge Weinfeld's dissent, we do not find either so compelling that the Commission was bound to accept it. Whatever hindsight may indicate would have been wise, the bondholders did not in fact seek dismissal of the reorganization proceedings until the spring of 1967; indeed they had been contending before the Commission that NH could survice as a freight-only railroad. See 331 I.C.C. at 659 (1967). And legislatures can hardly be expected to volunteer to assume large financial burdens so long as they have a reasonable expectation that part of these will be shouldered by a private corporation. Beyond this, as we pointed out in our previous opinion,

289 F. Supp. at 444, if inclusion of NH and PC had been found impracticable—or if, for that matter, if the PC merger had been disapproved by the Commission or after administrative approval had foundered in the course of the constituent roads had been unwilling to accept conditions that were imposed—"the NH bondholders would have had to shoulder losses between the date of such a determination and the grant of authority to abandon." The effect of what the Commission has done here is to assume that liquidation could have begun on January 1, 1968, a month before the PC merger had occurred and NH's right to inclusion thereby accrued. We see no inexorable logic that required the Commission to assume that liquidation could have started a year earlier when the *first* appeal in the Penn-Central merger had yet to be argued in the Supreme Court. In sum, we perceive no lack of reason in the Commission's assuming that a decision would not have been taken before January 1, 1967, and in postulating a delay of a year from the taking of a decision to liquidate for the time a proceeding under § 1(18) would necessarily entail.[3] Viewing the matter in a practical rather than a theoretical frame, what the Commission has done here was to select a fair date for shifting the heavy losses of NH's operation from the bonholders to PC—a judgment peculiarly in its province. We cannot say it went beyond bounds in assuming January 1, 1968, as the starting point of the liquidation, adding to the liquidation value (determined as of the

[3] We find little analogy in Tennessee Central Railway Company Abandonment of Operations, 333 I.C.C. 443 (1968), where an abandonment certificate issued in 3½ months. An all freight carrier with annual revenues of less than $4,000,000 is scarcely comparable with a passenger and freight carrier with annual revenues exceeding $100,000,000.

end of 1966) $5,000,000 on account of 1968 losses, and requiring a take-over at the end of 1968.

We cannot join our brother Weinfeld in reading our previous opinion, 289 F. Supp at 438, as precluding the Commission from postulating a one-year period after December 31, 1966, for an abandonment proceeding. What we rejected was a claim that we should allow for such a delay although the Commission then had not. Moreover, as the Remand Report pointed out, 334 I.C.C. at 58 a principal reason for our ruling was that, as matters then stood, the NH estate would be subject to a portion of operating losses for several years after consummation of the PC merger, whereas that burden has now been limited to eleven months. For whatever importance it may have, we likewise do not read the quotation from p. 5 of the joint brief of the Commission and the United States, cited in footnote 16 of the dissenting opinion, as our brother does. The "directive" was to make "detailed findings regarding the piecemeal liquidation value of the NH assets, as if an abandonment certificate were in hand on December 31, 1966"; we did not mean thereby to preclude the Commission from also considering whether or not it was reasonable to assume that such a certificate would then be in hand and making the necessary adjustment if it answered that question in the negative—any more than we meant to prevent the Commission from finding on remand, had it so chosen, that ten years rather than six would constitute a reasonable period for completing liquidation. If such a determination, which would diminish liquidation value by some $17.5 million, see 331 I.C.C. at 662, would have been within the Commission's power as it assuredly would, the instant one is equally so. The matter simply does not lend itself to the certainty that the bondholders assume.

The NH bondholders argue further that even if the Commission was justified in postulating a one-year delay in starting liquidation, its figures concerning the effect of this contain numerous errors. They say that if the date for starting liquidation is pushed forward a year, all properties will have to be revalued—presumably upward. PC responds that the failure to revalue has been beneficial to the bonholders, and that in any case far longer gaps between date of valuation and presumed date of sale have previously failed to stir objection. For example, the properties were all valued as of December 31, 1966, even though it was assumed they would not be sold then but over the six years following, and the same figures were also used in the study that assumed a ten-year program of liquidation sales. The bondholders argue also that non-operating property could be sold immediately, to which it is answered that the record affords no indication how much of this there is and that the Commission was warranted in assuming that, with their serious cash stringency, the NH trustees had done about all such selling that they could. The bondholders contend that sales contracts could be made on a contingent basis, that only sales scheduled for the first year would be delayed; and that the preservation costs would be less than estimated particularly since holders of defaulted equipment obligations would repossess. While these arguments are not without persuasiveness, they are offset by the Commission's failure to deduct a further year's depreciation of some $3 million by the conservativeness of the estimate that one year would suffice for an abandonment proceeding of such magnitude and possible judicial stays, and by the Commission's choice of

January 1, 1968 as the date for beginning liquidation instead of imposing on NH the costs of an additional year's delay in order to arrive at the possibly more logical starting date of February 1, 1969.[4]

Of the many issues in the case, the hypothetical question here posed is least susceptible to scientific determination. We cannot say that, all things considered, the Commission's basic assumption was irrational or its detailed findings unsupported by substantial evidence.

III. *The bulk-sale discount*

At the hearing on remand PC adduced the testimony of Mr. Robert E. Simon, an experienced real estate operator. The burden of this was that the appraisals of the sale of land in some 1700 parcels over a six-year period, discounted merely by 6% did not reflect certain elements of risk in such an undertaking, notably the likelihood that the liquidation might take longer than estimated and the possibility of an economic downturn, even though the appraisals had substantially marked down land remaining unsold at the end of the fourth year. Mr. Simon thought the proper measure of the value of the land was the price it would command if sold immediately to someone who would assume these risks. Such a person, he testified, would finance 75% of the purchase price by loans, which could not be obtained at less than 9% and would demand a 15% profit on his own investment for his entrepreneurial contributions and for undergoing the downside risks,

[4] Since inclusion was the alternative to abandonment and liquidation, it would not have been irrational to charge the NH estate with so much delay as would have occurred after the right to inclusion accrued, although not with more.

despite the possibility that even higher prices might be realized. Combining these figures to reach a composite of 10.5%, the Commission concluded that the land prices should be discounted by 4.5%; or $6.695 million, above the 6% previously deducted.

In the course of jutifying the deduction, the Commission said, 334 I.C.C. at 60, that "the liquidation value urged by the creditors assumes not only the immediate right to abandon . . . but also the right to break up the railroad and sell the parcels for their highest and best price" and that the latter right "may be restricted when a buyer for the entire bulk of the NH properties appears who will continue the operation of needed services." We entertain the gravest doubt concerning the legal premise underlying this argument; we would suppose that the constitutional right to abandon operations implies a right to break up the railroad and sell the parcels for their highest and best prices. Moreover we fail to see the relationship of this argument to Mr. Simon's testimony, which was not at all concerned with a buyer "who will continue the operation of needed service" but rather with one who would do precisely what the NH estate proposed to do.

However, the Commission also stated, "The bulk-sale discount merely reflects a market appraisal of the risks that the estate avoids, and the bulk buyer assumes," 334 I.C.C. at 61, and that the discount "fully recognizes, without conceding, NH's right to abandon and liquidate the estate." 334 I.C.C. at 63. While the Commission's language is not pellucid, we read this as saying that the Commission deducted the discount as a proper measure of risks not taken into account by the appraisals and the discount to present value. We cannot find this conclusion to be without rational

basis; the Commission was not bound to accept the testimony of a witness called by the bondholders that the discount to present worth was all that was needed. In addition to the factors emphasized by Mr. Simon, there is the fact, to which we have referred above, that the appraisals gave no effect to the serious adverse economic consequences from discontinuance of NH's operations, 331 I.C.C. at 667.[5] Corporations issuing securities pay substantial premiums for underwriting against the risk of market downturns even for relatively short periods,[6] and public utility commissions have considered the charges for such an underwriting as an element in the cost of capital in determining a fair return. See Bonbright, Principles of Public Utility Regulation 251-52 (1961); Garfield & Lovejoy, Public Utility Economics 124, 128 (1965). If it be thus prudent to guard against the risks of downturns over a period of a few weeks, we can hardly find it irrational for the Commission to have concluded that it would be imprudent for the NH estate to take this risk over a period of six years.

IV. *Alleged error in computing the liquidation value of N.H.*

A. *Grand Central Terminal Properties.*

In our previous opinion we concluded in effect that while no court had ever decided that NH was entitled to receive 50% of the surplus income of the GCT properties regard-

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[5] See also Exs NHI 44, pp. 11-12; NHI 97, p. 3; NHI 99, pp. 2–3.

[6] Except when the issue is first being offered to existing security holders an underwriter, like Mr. Simon's hypothetical bulk buyer, stands to make a profit from an upturn, in addition to his underwriting fee.

less of its cessation of operations, its claim to this was "exceedingly strong," 289 F.Supp. at 431. On remand the Commission made a conscientious effort to appraise the value of this share in surplus income and arrived at a figure of $28.887 million as against its former figure of $13 million and our guess of "at least $25 million," 289 F.Supp. at 432-33, which, however, did not take account of the proposed Tower building. The bondholders contend the figure to be too low; PC says it is too high. Our conclusions parallel those of the reorganization court.

The largest single item selected by the bondholders for criticism is the failure to credit NH with the value, estimated at $5.6 million annually, of NH's right to have its share of terminal expenses met by income from GCT properties. There is no question that this constitutes a significant benefit to PC as compared to a situation where the NH estate would share in GCT income and PC would be left with all the expenses—a situation we have previously found not to be within the language of the contracts or the probable intent of the parties. 289 F.Supp. at 430-31. But it does not follow that a capitalization of this amount constitutes an element of liquidation value of NH. Unless someone could be found to take over NH's operations into GCT, the right to have terminal income applied to expenses could not be sold to anyone even if the anti-assignment clause in the contract was not the obstacle that it may be. While it may well be that the State of New York would not allow all of NH's commuter services to disappear, there is no assurance in this respect and still less assurance that the State would operate into GCT if it had to pay the NH estate the full capitalized value of NH's right to set Terminal income off against Terminal expenses. Indeed, the

State, if it wished to continue using GCT, might well be able, either through its own bargaining position or the power of the ICC, to obtain a transfer of this right without making any payments to NH that would increase the "liquidation value" of this unique type of asset above the sum that could be realized if the State were not a buyer. 289 F.Supp. at 431. While we do not disagree with the bondholders' position that a state must pay the salvage value of property of a defunct railroad that it wishes to acquire, what is the "salvage value" of property that cannot be sold to anyone else and is of no value in the owner's hands? It is true, on the other hand, as we previously noted, 289 F.Supp. at 431, that cessation of all NH operations into GCT might affect the liquidation value of NH's interest by increasing *surplus* income by reducing total Terminal expense. But the bondholders offered no evidence on remand what this would be, and there are countervailing factors, such as probable decreases in concession income and expectable inflationary increases in Terminal expense over the years.

We are similarly unconvinced that the Commission acted without substantial evidence in estimating future hotel income at the average shown in the Terminal Account for the years 1964-67. There was a downturn from 1964 through 1966, while 1967 came near (although not up to) the level of 1964. The figures in the Terminal Account are net of capital expenditures, and a chief claim of the bondholders is that these could have been removed and deduction made only for what would be appropriate under depreciation or retirement accounting. The Terminal Account in this respect only reflects the long-standing practice of the parties, which is embodied in the hotel leases them-

selves. Beyond this, the Commission was justified in concluding from the absence of any trend in Terminal Account earnings from 1960 to 1967 that the annual capital expenditures on these old hotels, however described from an accounting standpoint, constituted regularly recurring costs necessary to maintain income rather than likely to increase it. 334 I.C.C. at 36-38.

Another bone of contention, not dealt with in our previous decision, concerns a lease recently negotiated by PC of the air rights over Grand Central Station for the construction of an office building. PC stipulated that if this were built, it would bring an annual income of $2.3 million or under "certain favorable circumstances" $3 million, beginning about 4 years after the commencement of construction. Prior to the completion of construction the annual rental would be $1 million, but a deduction from this figure must be made for the transfer to the lessee by the railroads of concession rights worth $700,000 a year, and for certain other expenses. Although the Commission considered the question "whether the proposed building is so speculative that no value can be assigned to it," it concluded that "it is probable that the building will eventually be constructed," but only after long delay. 334 I.C.C. at 34. It assumed accordingly that the full rental of $2.3 million would not be realized until 10 years from the valuation date of December 31, 1966. This resulted in a discounted figure of $1,280,000; capitalization of NH's 50% share at 8% produced a valuation of $8 million.

The bondholders complain over the failure to take account of any part of the $1 million annual rental during construction and use of the $2.3 million rather than the $3 million figure thereafter. But, apart from the absence

of proof that the latter figure was fairly expectable, any conservatism on these scores was a reasonable offset for the meagre weight given to the doubt whether the building would be constructed at all. Indeed we consider PC's grievances with respect to the Tower Building considerably more impressive than the bondholders'. While we would have had no objection if the Commission had handled the matter as our brother Weinfeld ingeniously suggests, we see no basis for compelling this.

The only other item relating to GCT requiring discussion is the Commisison's refusal to require PC to pay NH its share of surplus income for 1967 and 1968. The justifications for this refusal were that to make the payment "would be giving the claim a double value, once as a dollar claim and secondly as the capitalized value of its claim as of December 31, 1966"; that the bondholders were in effect seeking to move the valuation date forward; and that in that event the Commission "would also have to make other adjustments, such as depreciation for 1967 and 1968; and such revaluation of the estate might be quite different from the ultimate liquidation figure we have found." 334 I.C.C. at 38-39.

Such arguments misconceive the nature of the bondholders' claim, which is simply that they are entitled to receive whatever their property earned while they still owned it. Only if PC had paid NH for the assets on the valuation date could it properly argue that the bondholders were trying to recover twice by laying claim to the earnings of those assets while they also retained the interest paid on the sum given in exchange for them. When the assets were valued, and what they were valued at, is beside the point.

B. *Harlem River and Oak Point Yards.*

After careful reexamination the Commission adhered to the $18,090,990 appraisal submitted by the NH Trustees "as representing the value of the yards in the event NH were liquidated and its line of railroad dismantled." 334 I.C.C. at 41-48. Judge Anderson has sustained the bondholders' claim for a higher appraisal of $22,650,000, which assumed that all the industries in the two yards would enjoy the present level of rail service. The principal argument for this is founded on the premise that, in the event of liquidation of NH, PC would be obliged to continue service over its Port Morris branch to the Hunts Point Wholesale Market which is located north of, but not adjacent to, the Oak Point yard. Acceptance of the premise would not necessarily entail the conclusion necessary to compel adoption of the higher figure. The Commission's evaluation of the probable scope of future rail service to these properties in the event of liquidation of NH lies in an area peculiarly within its expertise, and we decline to disturb it.

C. *NH's interest in the Boston & Providence.*

In our previous opinion we held that the liquidation value of NH's interest in the Boston & Providence was $5.8 million, a figure readily derived by subtracting from the $8.1 million appraised net liquidation value of B & P's physical assets the $2.3 million in cash that NH would have to pay for the publicly held stock of that company. 289 F.Supp. at 434-35. Despite the seeming simplicity and correctness of that calculation, the Commission on remand, while rejecting the bondholders' contention that a much higher price was justified by current market quotations for

a few CCBI's,[7] achieved a somewhat higher one of its own, 334 I.C.C. at 50-52. It started with the $2.3 million NH would concededly have to spend in buying up the 20,000 publicly held shares of B & P. The Commission then assumed that 20,000 shares it said NH already owned must be worth the same amount. To the resulting $4.6 million it added $5 million for the value of outstanding B & P debentures owned by NH, resulting in a $9.6 million total. Since by hypothesis the value of the B & P securities could not be greater than the value of the physical assets underlying them, which had previously been set at $8.1 million, the Commission felt that the missing $1.5 million must be the value of the CCBIs, which represented a potential that had not been taken into account in the asset valuation study because it was thought too speculative.

Although we do not question the conceptual soundness of taking market price of securities as a rough guide to asset value, it appears that the $2.3 million figure was not based on the market's estimate of B & P liquidation value, but on the Commission's rough guess at it. Boston & Providence RR. Corp. Reorganization, 327 I.C.C. 10, 20-21 (1966). Furthermore, we cannot find any evidence that the debentures were worth $5 million. In fact, the United States, to which they were pledged during the 1950's by NH as the sole security for loans that greatly exceeded their face value, agreed to exchange them for NH securities with a face value of $3.5 million, and this plan has been judicially approved as a fair compromise between the face amount of the B & P debentures and the well-supported view that because NH was in fact the primary obligor on the deben-

[7] For the nature of these securities, see 289 F.Supp. at 434–35.

tures, the obligation was extinguished as soon as NH acquired them in 1954. In re Boston & Providence RR Corp., 260 F.Supp. 415, 421-22 (D.Mass. 1966). It also appears that NH in fact did not own the 20,000 shares of B & P stock which the Commission claims for it but with only 16,000, with most of the missing 4,000 being held by the debenture sinking fund. Boston & Providence RR Corp. Reorganization, 327 I.C.C. 10, 13 (1966).

If we were to retain the Commission's approach, while correcting the errors just noted, we would come out with a value for B & P very close to, but slightly below, the $8.1 million of the liquidation study. This study, however, was the result of detailed examination of the B & P properties, its findings have never been seriously disputed, and it would be irrational to make what amounts to a minor adjustment in its findings on the basis of assumed values for stock and securities that are far more speculative than the estimates they would be used to correct. We therefore adhere to our previous determination.

D. *Deduction for accrued real estate taxes.*

In our last decision we found the Commission had made a double deduction for $16.2 million of accrued real estate taxes on property required to be transferred free of liens by also including these in the assumed expenses of liquidation. 289 F.Supp. at 438. On remand the Commission decided that "the proper treatment of this item is to remove it from the liquidation expenses." 334 I.C.C. at 40. However, the Commission increased liquidation value by only $14.6 million on the theory that under the NH reorganization plan such taxes are to be paid off by notes which the market would discount by 10 to 12 percent. 334 I.C.C. at 41.

We see no sufficient basis for this. There is no assurance that the holders of the tax liens will accept the notes offered in the NH reorganization plan, and they would seem to have little motive to do so now that NH no longer needs to conserve cash in order to keep operating a railroad.[8]

E. *Net Additions and Betterments between December 31, 1966 and December 31, 1968.*

The bondholders claim that the purchase price should be increased by net increases in NH's property accounts since the valuation date, December 31, 1966. The Commission contends that the point was not raised before it; the bondholders deny this. We find it unnecessary to pass upon the issue since we are satisfied with the answer made by the Commission and PC on the merits, namely, that acceptance of the bondholders' contention would require a complete revaluation of the property. Two examples will suffice to illustrate this. Many of the expenditures were improvements to the right of way which, however necessary for continued operation, might add nothing (or even be a negative factor) if the road were to be scrapped. Another is that if an upward allowance were to be made for net additions to the property accounts since December 31, 1966,[9] a down-

[8] Similar considerations apply to PC's contention that the Commission should have credited it with $1.2 million of post-bankruptcy interest on the accrued taxes which the NH estate will not have to pay in reorganization. Nicholas v. United States, 384 U.S. 678, 686 (1966).

[9] This is an appropriate place to say that we have considered the bondholders' attacks on the depreciation adjustment for 1966, 334 I.C.C. at 47–50, but find no force in them sufficient to justify a remand. The bulk of the $3.253 million adjustment, $2.367 million, relates to equipment, where depreciation would decrease liquida-

ward adjustment would have to be made for depreciation insofar as this would affect liquidation value. Since we have already sustained the Commission's choice of a valuation date for the reasons given in Part II, we decline to order any adjustments inconsistent with that choice.

F. *Failure to reduce discount to present worth to reflect price reductions.*

The bondholders contend that the Commission reduced the estimated prices to be obtained for portions of NH's property, but did not correspondingly reduce the discounts used in determining the present worth of what the NH estate would receive. The logic of this position is apparent, and we shall ask the Commission to take appropriate account of it in the decree to be submitted to us.

V. *Loss Sharing*

In our previous opinion we accepted "the Commission's view that it was not bound to require Penn Central to assume all losses of NH subsequent to the Penn Central merger" and held that "the Commission was justified in setting a ceiling on Penn Central's participation in losses and in providing that it bear only a fractional share." 289 F.Supp. at 443-44. We disapproved its formula with respect to loss-sharing only because the downward progression of PC's share in the second and third years might have, and indeed was intended to have, the effect of discouraging

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tion value. Such merit as exists in the bondholders' argument that depreciation would not necessarily affect liquidation value thus applies only to such part of the $866,570 for "Other Property" as related to items like ballast (in contrast to rails and ties) that would not be sold as such.

the bondholders from pressing legitimate claims, 289 F.Supp. at 444-45. The direction for inclusion of NH on December 31, 1968, eleven months after the PC merger, mooted the question of loss sharing for subsequent years, and the Commission adhered to the portion of its formula requiring PC to absorb all 1968 operating losses up to a maximum of $5.5 million—or $5 million for the 11 months, 334 I.C.C. at 71-74. In light of the legal views expressed in our last opinion, which we see no occasion for altering, this was well within the area confided to the Commission's judgment. This is particularly true in light of the Commission's decision to advance the burden of actual inclusion to December 31, 1968.

VI. *The consideration payable by PC*

The bondholders make two attacks on the valuation of the consideration payable by PC. One of these is of minor, the other of major significance.

In our previous opinion we recognized the force of the position of the Trustee of the First Mortgage securing the Harlem River Division bonds that these bonds should be accorded special treatment because of their fully secured nature, but considered this to be "a matter left to the reorganization court." 289 F.Supp. at 442. That court agreed with the view we had tentatively expressed. 289 F.Supp. at 464. The Commission accordingly directed PC to assume the bonds, and said that the value to NH of having this obligation removed would be $8.9 million. 334 I.C.C. at 70-71. The bondholders say that this figure was derived by simply adding the face value of the principal, which is $6.6 million payable January 1, 1973, to the face value of the

accrued interest, which is $2.3 million payable in five equal annual installments between 1969 and 1973, without making any deduction for the delays in payment. We accept this criticism, and direct the Commission to modify its order by calculating an appropriate discount.

A much more important issue is the Commission's adherence to a valuation of $87.50 per share for PC stock. Although we sustained this in our previous opinion, 289 F.Supp. at 436-37, the market's evaluation of the stock has drastically changed for the worse since that time. Whereas we noted that while that opinion was being written, PC stock had advanced to $85 per share, and it reached a high of $86.50 on July 14, 1968, it had declined to $69.75 by August 13, 1968, when the reorganization court rendered its decision also sustaining the $87.50 figure, to $63.375 on the dates of the Remand Report and of actual inclusion, and still further thereafter. The decline during the last half of 1968 was the more significant in view of the fact that the Dow-Jones rail average on December 31, 1968, was at approximately the same level as on the date of our decision.

On the hearings on remand the bondholders called an expert witness who testified to a "current investment value" of $65 per share. In a footnote constituting its sole discussion of this important problem, the Commission noted that the witness "was unfamiliar with Penn Central's operating and financial plans and condition; gave undue weight to extraordinary expenses of the past; and generally neglected the future prospects of the company." 334 I.C.C. at 68 n. 40.

Our views on this subject parallel those recently expressed by the reorganization court. The NH trustees had asked for

inclusion of NH in the PC System. It must have been expected from the outset that a large portion of the purchase price would consist of PC stock and that this would not be immediately sold but rather would be held by the reorganized NH as a major long-term participant in what was expected to be a great and successful railroad system.[10] Spot fluctuations are therefore not decisive, especially when, as here, there are reasonable explanations for them, such as the unanticipated difficulties in working out the operating details of the merger and the prospect of PC's having to shoulder NH losses at an earlier date and in larger amounts than had been anticipated. A reasonable time should thus be accorded to determine what the real value of PC stock is. On the other hand, in the last analysis the market is the true appraiser and, if anticipations, no matter how well founded, should not be achieved, a proper adjustment should be made. We find Judge Anderson's solution of this difficult problem to be admirable and direct that the order be modified as provided in his opinion.

We referred in our previous opinion to the "unfortunate" character of "the duplicitous system of review" by this court and the reorganization court. 289 F. Supp. at 424-25 & n. 3. Now this appears all the more unfortunate in light of the different conclusions the two courts have reached on important points. We regret our inability to agree fully with Judge Anderson, for whose views, reflecting years of devoted service to the administration of the

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[10] This position is illustrated by the proposal of the Trustee under NH's junior mortgage that the added consideration receivable by NH as a result of departure from the Trustees' contract should largely take the form of PC stock.

NH estate, we entertain the greatest respect. We also regret our inability to accept positions forcefully expressed by our esteemed dissenting colleague. Essentially, we think our disagreements with Judge Anderson and Judge Weinfeld reflect a difference in view concerning how far we are at liberty to substitute our own notions for the decisions the Commission has taken in what we regard as a sincere effort to comply with the tasks both courts assigned it on remand. In any event we must decide the case according to our own lights; reconciliation of divergent views will come ultimately in the nation's highest court, which alone can speak with authority.

The Commission is directed promptly to prepare and serve a proposed decree which, among other things, shall reflect in dollar amounts the changes directed in this opinion. Increases or decreases in the price shall be in approximately the same ratio as the figures for PC stock, PC bonds and cash in the Remand Report, 334 I.C.C. at 71, bear to each other. Other parties may serve counter-proposals within ten days thereafter, and a further five days will be allowed for comments on such counter-proposals.

/s/ HENRY J. FRIENDLY
U.S.C.J.

/s/ RICHARD M. LEVET
U.S.D.J.

June 18, 1969.

WEINFELD, D. J. (dissenting in part):

On the last round, when the Commission found that $125 million was "at least equivalent to the liquidation value" of

the New Haven assets,[1] both the Reorganization Court and this Court disagreed with that finding and remanded the matter to the Commission to correct substantial error.[2]

[1] Second Supplemental Report of the Commission on Further Hearing, 331 I.C.C. 643, 697 (1967).

[2] New York, N.H. & H.R.R. First Mortgage 4% Bondholders Committee v. United States, 289 F. Supp. 418 (S.D.N.Y. 1968) (three-judge court); In re New York, N.H. & H.R.R., 289 F. Supp. 451 (D. Conn. 1968) (reorganization court). This Court's remand related to the following:

(1) the Commission's failure to discount New Haven's liquidation expenses over the projected six-year liquidation period, 289 F. Supp. at 427–28;

(2) its miscalculation of New Haven's right to surplus income from the Grand Central Terminal properties, *id.* at 428–33;

(3) its ambiguous valuation of the Harlem River and Oak Point freight yards, *id.* at 433–34;

(4) its erroneous valuation of New Haven's interest in the Boston & Providence Railroad, *id.* at 434–35;

(5) its failure to discount the 5% bonds with which Penn Central was to meet its obligations under the Purchase Price Adjustments, *id.* at 437–38;

(6) its error in deducting from the amount to be paid to New Haven the sum of outstanding real estate tax liens, *id.* at 438;

(7) its failure to indicate the source of its estimate of 1966 depreciation of New Haven properties, set forth in its brief before us but not in its Inclusion Report, *id.* at 438;

(8) its miscalculation of the cost to Penn Central of Penn Central's 5% bonds, its assumption of New Haven's obligations under the Boston & Providence mortgage, and its payment under the Purchase Price Adjustments, *id.* at 439;

(9) the Commission's failure to take into account a reduction in 1966 New Haven equipment obligations, *id.* at 439 n. 15;

(10) its conclusion that Penn Central would assume overmortgaged New Haven equipment, *id.* at 439;

(11) its failure to include any of Penn Central's absorption of New Haven's interim operating losses in the category of the cost of acquisition to Penn Central, *id.* at 440;

The Reorganization Court considered that the Commission had understated the value of the New Haven properties by $33 to $55 million;[3] this Court, by $45 to $50 million.[4] In its latest report, the Commission restored some $37.7 million in value and then reduced that amount by $22.1 million.[5] In effect, it gave with one hand and took away with the other. The net result is it has increased the amount to be paid for New Haven's assets by $15.6 million, despite the Reorganization Court's then view that any sum below the $33 to $55 million range "would be unfair and inequitable to the creditors . . . ."[6]

I recognize, of course, that the scope of review of this Court of the Commission's order is limited; but I also recognize that the Court's function in reviewing the Commission's order is "to guard against the possibility of gross error or unfairness."[7] Because I am satisfied that the Commission's current findings and conclusions lack substantial evidentiary support and contain more than a "possibility" of, but again are pockmarked with, gross error and unfair-

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(12) its use of a sliding-scale formula for Penn Central's interim loss-sharing as a device to curtail litigation by the New Haven bondholders, *id.* at 444; and

(13) its tendency to "round off" sums, with a consequent loss of some $5.3 million to the New Haven estate, *id.* at 427.

[3] 289 F. Supp. at 465.

[4] *Id.* at 440.

[5] Fourth Supplemental Report of the Commission on Reconsideration and Further Hearing, 334 I.C.C. 25, 53, 63 (1968) ("Remand Report").

[6] 289 F. Supp. at 465.

[7] Penn Central Merger and N & W Inclusion Cases, 389 U.S. 486, 524 (1968).

ness, I respectfully dissent with respect to the matters hereafter discussed.

The Reorganization Court and this Court appear in agreement that New Haven is entitled to the fair liquidation value of its assets transferred to Penn Central. My disagreement with my brethren of this Court centers about their acceptance of the Commission's "other pricing considerations" which result in reducing substantially below liquidation value the amount to be paid for the New Haven assets.[8] After finding that the liquidation value is $162.7 million, the Commission decides it is not "fair and equitable" for Penn Central to pay this sum to New Haven based upon these "other pricing considerations," which are: first, a $15.386 million deduction for a year's delay that would have ensued had the New Haven applied for a certificate of abandonment; second, a $6.695 million reduction for a forced bulk sale of the New Haven assets instead of a piecemeal liquidation over a six-year period.[9] Each deduction, the Commission says, in effect reflects an application of the liquidation hypothesis. Each is justified by the Commission under its claimed authority to place a limitation on New Haven's right to abandon operations and to compel the sale of the assets in bulk as if in fact an abandonment had occurred.[10] The majority uphold the one-year abandonment delay deduction—which by itself eliminates nearly one-third of the value that we suggested on the remand the Commission restore—on the ground it represents the product of the Commission's expertise in

[8] 334 I.C.C. at 53.

[9] *Id.* at 54, 60, 62.

[10] *Id.* at 57, 62–63.

fleshing out the details of the hypothetical liquidation situation.

Deduction for one-year abandonment delay.

The history of these proceedings shows that December 31, 1966, was accepted by the parties and the Commission as the date on which a six-year liquidation was hypothesized to commence. The date thus does not represent, as the majority suggest, the date "the liquidation *decision* is assumed to have been taken." (Emphasis supplied) The abandonment delay concept in practical terms adds another year to the six-year liquidation period.

Although the expenses of the six-year liquidation were provided for in the prior report, the Commission did not then include any deduction for abandonment proceeding delay.[11] Support for the Commission's deduction of $15.386 million based on the added one-year abandonment concept, is claimed because the bondholders failed to apply for a certificate before the spring of 1967 and allegedly waived their right to liquidation value. The record does not support this claim. Always central to the merger was the inclusion of the bankrupt New Haven. Were this not the fact, an abandonment proceeding would have been compelled in the light of the year-by-year losses and the constant erosion of the bankrupt estate, with a favorable determination foreordained.[12] The Reorganization Court

[11] 331 I.C.C. at 662.

[12] True, the states, communities and other interested parties would have been entitled to be heard in opposition to any application, and perhaps the proceeding would have dragged on; but even so, and despite the Commission's view that Brooks-Scanlon Co. v. R.R. Comm'n, 251 U.S. 396 (1920), has been overruled sub silentio, New Haven could not have been compelled constitutionally, year after year, to absorb the constantly increasing operating losses

has fully set forth, in its rejection of the abandonment delay concept, incontrovertible facts that expose the lack of substance to the contention that the failure to apply for a certificate of abandonment before 1967 worked a waiver of the bondholders' rights to the full liquidation value. Indeed, as Judge Anderson, the one most familiar with these proceedings since their inception, has so convincingly demonstrated, but for Penn Central's commitment to take over New Haven as an operating entity, and the universal understanding that such would be the case, abandonment proceedings would have begun and terminated well before the end of 1966.[13] To suggest otherwise flies in the face of this record.

Penn Central, in seeking to uphold the Commission, urges that the added cost of delay is merely an "adjustment"[14] that the Commission did not find necessary to pursue once it set the price stipulated in the Purchase Agreement. The argument for such a delay discount was advanced on the prior round and rejected by this Court. We relied upon the fact that "a considerable portion of the [interim] losses [would] . . . be borne by the NH estate" in rejecting the claim that "before the NH Trustees could even begin a liquidation, lengthy abandonment proceedings would be required, during which large cash losses would be incurred and the property would further depreciate."[15]

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or its security holders deprived of their right to foreclose their liens. And while one need not quarrel with the Commission's position that a deficit-ridden railroad has no *immediate* right to abandon operations and dismantle, this does not mean that the public interest can compel such a railroad to continue its loss operation indefinitely.

[13] In re New York, N.H. & H.R.R., —— F. Supp. ——, —— (D. Conn. May 28, 1969); 289 F. Supp. at 456-57.

[14] Penn Central Answering Brief at 26.

The Commission itself understood the true significance of the December 31, 1966 valuation date, as is evidenced by its brief before us on this round. "The [remand] report," it says, "makes detailed findings regarding the piecemeal liquidation value of the NH assets, *as if an abandonment certificate were in hand on December 31, 1966, in accordance with the directive of the Three-Judge Court.*" [16]

In essence, the Commission's abandonment-delay concept envisions a one-year "freeze" on the New Haven's liquidation program, while proceedings drag on before the Commission and the courts. According to the Commission, the only development during that year would be a further deterioration in the financial status of the New Haven. That was not the Commission's position on the last round. Then, in observing that a large portion of the New Haven's assets consisted of land, it said: "We cannot assume that these values will diminish. It is at least as reasonable to presuppose that the values will increase." [17] That was our position, too. We thought that "[i]f we were to posit a liquidation beginning only some years hence, we could not simply deduct interim cash losses and depreciation but would have to ask the Commission to revalue the assets and this might yield a higher price." [18]

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[15] 289 F. Supp. at 438.

[16] Joint Brief of the United States and the Interstate Commerce Commission at 5. (emphasis supplied)

[17] 331 I.C.C. at 698.

[18] 289 F. Supp. at 438-39. The fact, relied upon by Penn Central, that the record contains no evidence to indicate what the added value might be, is hardly the fault of the bondholders. The Commission made clear, both in its Remand Report and in oral argu-

Upon this record, the abandonment delay concept, which deducts $15.386 million from the liquidation value of New Haven assets, is without justification and is not based upon substantial evidence.

Bulk sale concept.

The bulk sale concept, a theory not previously considered by the Commission, is based upon its view that "we may compel the bulk sale and the bulk sale discount as a condition of an abandonment certificate, and, therefore, as a reduction of the present price." [19]

The Commission, by hypothesizing a forced bulk sale of New Haven's assets to an entrepreneurial operator based upon his borrowing of 75% of the capital at 9% and earning a 15% return on his equity investment—and then applying a discount factor of 10.5% over the six-year liquidation period—further reduces the amount to be paid to New Haven by $6.695 million.[20] This theory deprives the bondholders of the salvage value of their property anticipated under the six-year liquidation program and at once raises constitutional issues. The expenses under the six-year liquidation program, which contemplated the sale of the properties on an individual basis, are $24.149 million, which include not only the cost and expense of a piece-by-piece sale of the assets, but a sum to cover the sale of some of the property below fair market value, as well as the risk

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ment before us, that it did not regard the question as a matter for evidence. 334 I.C.C. at 29; Minutes of Oral Argument of April 17, 1969, at 139-41.

[19] 334 I.C.C. at 61.

[20] *Id.* at 62.

of non-sale.[21] To make another deduction of more than $6 million under the bulk sale theory is an unwarranted duplication of part of the expense already charged to the New Haven.

Although my esteemed colleagues are compelled to "entertain the gravest doubt concerning the legal premise" upon which the Commission postulated its theory, they purport to find justification for its acceptance by culling other statements from the Commission's report and deducing therefrom what the Commission really intended, to wit, a "discount as a proper measure of risks not taken into account by the appraisals and the discount to present value." Passing for the moment that this is not at all the theory relied upon by the Commission, which at once raises a question as to whether the agency action can be upheld,[22] the theory, when tested on the basis of what the Commission did, as opposed to what it might have done, is clearly erroneous and cannot prevail. The Commission's determination rests upon its assumed power to compel the bulk transfer to assure "the continued operation of the property and preservation of its unity."[23] However, the evidence upon which it justified the bulk sale deduction contemplated the sale of the real estate to a private developer who was in no way committed to the "continued operation of the property and preservation of its unity."[24]

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[21] 331 I.C.C. at 662.

[22] SEC v. Chenery Corp., 318 U.S. 80, 94 (1943).

[23] 334 I.C.C. at 61.

[24] R–29; T. 29799 et seq.

Grand Central Tower Building.

As to the proposed lease of the air rights for the construction of the Tower Building, which if in fact constructed would eventually bring an annual income of $2.3 million, or under "certain favorable circumstances," $3 million, the Commission, while aware that the prospect of actual construction was speculative, nonetheless concluded "it is probable that the building will eventually be constructed. . . ." [35] Purportedly it resolved the probability in favor of the bondholders. Whether or not the project goes forward depends upon local action, much of it subject to variant community interests. No one can be certain what action the City Planning Commission, the Landmarks Preservation Commission or other official agencies will take with respect to the proposal.[36] The existing heavy density of the area, the excessive land coverage and the already overburdened and inadequate municipal and private facilities there could well lead to a rejection of any zoning variations. Other forces, including representative civic groups whose judgment has in the past carried great weight with official bodies, are also in the picture. With the matter shrouded in much uncertainty and the subject of sharp public controversy, any decision which purports to value New Haven's interest may work unfairly to Penn Central or New Haven. Until there is further clarification of the future of the Tower Building, I think the situation lends itself to the use of certificates of contingent beneficial interest (CCBI's). The Commission's

[35] 334 I.C.C. at 34.

[36] The Commission itself, with respect to New Haven's Bronx freight yards, noted that action by the Planning Commission on a proposed zoning change was too speculative a basis for fixing valuation. 334 I.C.C. at 41; 331 I.C.C. at 668.

judgment that it is probable that the building will eventually be constructed may prove to be sound; then again, it may not. While I agree with the Commission that it is desirable that the rights of the parties be determined and the issue put to rest, there is at this time lacking a factual basis for a fair and equitable determination, and accordingly the CCBI's offer a solution to this vexing problem.

Stock valuation.

The Commission valued 950,000 shares of Penn Central stock at $87.50 per share, purportedly worth $83.1 million at the time of inclusion, as part of the consideration to be received by New Haven. The Reorganization Court and this Court agree that by the reality of the market place, "the true appraiser," the stock is grossly overvalued—at the date of inclusion by some $23 million. The problem admittedly is a difficult one. The Reorganization Court proposes an imaginative solution which is acceptable to my brethren. With the utmost respect to them, I do not believe this is the solution. In my view it is more desirable to remand to the Commission for further consideration and to afford all interested parties an opportunity to submit proposals. The question of the stock valuation appears to have received little or inadequate consideration by the Commission. As my brethren note, the sole discussion of this important problem was a rather cavalier brush-off of the bondholders' challenge to the Commission's valuation of the stock at $87.50 per share.[27] The New Haven estate is entitled to the equivalent of $83.1 million as part of the purchase price. After hearing the parties upon a remand,

[27] 334 I.C.C. at 68 n. 40.

the Commission may require the issuance of a larger number of shares or otherwise provide for that sum.

Losses from February 1, 1968 to December 31, 1968, the inclusion date.

The Commission limits the loss that Penn Central is to bear to $5 million.[28] Consistent with my view previously expressed, the entire interim operating losses should be borne by Penn Central.[29] Its argument that it should not be charged with losses over which it has no control is stripped of much of its force, since it had the opportunity, which it declined for reasons which even the Commission thought unpersuasive, to participate in a joint effort to achieve economies during the interim period.[30]

Harlem River and Oak Point Yards.

The Commission reaffirmed that its acceptance of the $18.1 million appraisal was based upon the assumption that "NH's railroad system on liquidation would be entirely dismantled, including the approximately 2 miles of main-line tracks connecting the two yards, which are not immediately adjacent."[31] The Commission's equivocal statement that "[i]t is extremely doubtful that railroad service would continue to the Harlem River and Oak Point yards if NH's system were liquidated" is far from persuasive.[32] Its find-

[28] *Id.* at 74.

[29] 289 F. Supp. at 448–49 (concurring opinion).

[30] 331 I.C.C. at 712-13.

[31] 334 I.C.C. at 43.

[32] *Id.* at 44.

ing as to non-operation of the yards made with respect to Penn Central, any existing terminal carrier, a new terminal carrier or the City of New York does not appear to be based upon substantial evidence. It is difficult to agree that an important rail service to industrial users would be terminated and the line dismantled. Nothing in the record supports the Commission's assumption that the properties would be stripped of their trackage and electricity, both highly desirable industrial features, and the former alone commanding about a 10% premium in Bronx realty values. The Commission's finding of value of $18.1 million is without substantial evidential support, particularly in the light of the appraiser's testimony as to the incorrect basis of his lower valuation; at the minimum, the value is the higher of his appraisals, $22.650 million.[33]

It is regrettable that these proceedings now pending for more than a decade, cannot be terminated. But the errors in the Commission's report here under review are so egregious as to leave no alternative other than to remand for further consideration.

EDWARD WEINFELD
United States District Judge

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[33] T. 28849, 28864.

Memorandum Decision of the Three-Judge Court on the Decree

THE NEW YORK, NEW HAVEN AND HARTFORD RAILROAD COMPANY FIRST MORTGAGE 4% BONDHOLDERS COMMITTEE, THE CHASE MANHATTAN BANK, N.A., as Trustee Under the General Income Mortgage of the New York, New Haven and Hartford Railroad Company, MANUFACTURERS HANOVER TRUST COMPANY, as Trustee of the First and Refunding Mortgage of the New York, New Haven and Hartford Railroad Company, and OSCAR GRUSS & SON,

Plaintiffs,

v.

UNITED STATES OF AMERICA and INTERSTATE COMMERCE COMMISSION,

Defendants,

PENN CENTRAL COMPANY, STATE OF NEW YORK, and STATE OF CONNECTICUT,

Intervening Defendants.

UNITED STATES DISTRICT COURT

S. D. NEW YORK

Nos. 68 CIV. 5200, 5210

69 CIV. 11, 12

MEMORANDUM

The serious disagreements that have characterized other aspects of these proceedings have continued with respect to the form of decree appropriate to carry out our opinion

of June 18, 1969. We find that none of the decrees submitted is wholly satisfactory and have therefore fashioned our own from them. We believe that what it contains and what it does not sufficiently indicate our views concerning the many contentions, with one exception.

This concerns our adoption of the Commission's computation of $410,000 as a reduction in the discount to present worth. See 334 I.C.C. at 529-30 and Item A-2 in the decree. The NH bondholders contend that, in addition to this sum, which they concede to be arithmetically correct for the items listed in the Commission's report, there should be a further reduction of $2,695,899. The basis for this was explained in a letter dated June 17, 1969, to the reorganization court and was adopted by it in an order dated July 28, 1969. We have not passed on the merits of this contention since we do not consider it to be appropriately before us on settlement of the decree. The difference in the treatment of this item by the two courts will be another matter for ultimate resolution by the Supreme Court.

/s/ HENRY J. FRIENDLY
U.S.C.J.

/s/ RICHARD H. LEVET
U.S.D.J.

September 11, 1969.

Decree of the Three-Judge Court Sustaining the Commission's Fourth Supplemental Report With Modifications, dated September 11, 1969

THE NEW YORK, NEW HAVEN AND HARTFORD RAILROAD COMPANY FIRST MORTGAGE 4% BONDHOLDERS COMMITTEE, THE CHASE MANHATTAN BANK, N.A., as Trustee Under the General Income Mortgage of the New York, New Haven and Hartford Railroad Company, MANUFACTURERS HANOVER TRUST COMPANY, as Trustee of the First and Refunding Mortgage of the New York, New Haven and Hartford Railroad Company, and OSCAR GRUSS & SON,

Plaintiffs,

v.

UNITED STATES OF AMERICA and INTERSTATE COMMERCE COMMISSION,

Defendants,

PENN CENTRAL COMPANY, STATE OF NEW YORK, and STATE OF CONNECTICUT,

Intervening Defendants.

UNITED STATES DISTRICT COURT

S. D. NEW YORK

Nos. 68 CIV. 5200, 5210

69 CIV. 11, 12

The Interstate Commerce Commission having on November 25, 1968 (service date December 2, 1968) issued its Fourth Supplemental Report and Order in consolidated

proceedings before the Commission in Finance Docket Nos. 21989, 21990, 24361, 21669 and 24756, and the plaintiffs herein having each instituted an action pursuant to 28 USC §§ 1336, 1398, 2284 and 2321-2325, to annul, enjoin and set aside the Fourth Supplemental Report and Order except insofar as said order directs Penn Central Company to acquire substantially all of the assets and operations of The New York, New Haven and Hartford Railroad Company no later than December 31, 1968 and to pay the consideration required by said Fourth Supplemental Order, and the said actions having been consolidated by an order dated January 10, 1969 and a United States District Court for the Southern District of New York consisting of three Judges having been convened pursuant to 28 USC §§ 2284, 2321-2325 by order dated January 10, 1969 to decide the said consolidated actions, and issue having been joined by the filing of answers on behalf of the defendants and the intervening defendants, and all parties having had a full opportunity to submit briefs on the issues, and the issues having come on for hearing on April 17, 1969, and all parties in interest having been heard or having been given an opportunity to be heard, and the Court being duly advised in the premises and having, on June 18, 1969 filed its opinion (Friendly, C.J. and Levet, D.J.) and a dissenting opinion having been simultaneously filed (Weinfeld, D.J.) and the opinion of the Court having set forth Findings of Fact and Conclusions of Law, and the Court thereafter having been advised by the Interstate Commerce Commission by its Fifth Supplemental Report dated July 10, 1969 and the other parties having submitted comments on the several issues discussed in said Fifth Supplemental Report and on the proposed decree, and the Interstate

Commerce Commission by order dated August 26, 1969, having supplemented and modified its Fifth Supplemental Report and proposed decree in light of such comments,

NOW, THEREFORE, it is hereby ORDERED, ADJUDGED and DECREED:

A. That the consideration to be paid to the New Haven Railroad by Penn Central Company as set forth in the Commission's Fourth Supplemental Report be and it hereby is increased in the net amount of $990,000 as a result of the following:

1. An increase of $1,600,000 representing an adjustment in the treatment of accrued real estate taxes;

2. An increase of $410,000 representing an adjustment to the discount to present worth arising from decreases in valuation of properties of the New Haven Railroad;

3. An increase of $480,000 representing the amount by which the Commission overvalued the assumption by Penn Central Company of the obligations of the New Haven Railroad in respect of its Harlem River Division Bonds; and

4. A decrease of $1,500,000 representing the overvaluation of the New Haven Railroad's interest in the Boston & Providence Railroad Corp.;

B. That the said additional consideration of $990,000 shall be paid, as provided in the Commission's revised Fifth Supplemental Report served August 28, 1969, in the following manner: 57.1% of such additional consideration by the issuance and delivery of Penn Central common

stock together with all rights to dividends payable on such stock from December 31, 1968 as if such stock had been issued and delivered on that day; 37.4% by the issuance and delivery of 25-year Divisional First Mortgage Bonds bearing interest at 5% (principal amount in a ratio of 23/20) together with interest at 5% from December 31, 1968; and 5.5% in cash with interest from December 31, 1968 at the rate of 6%;

C. That Penn Central Company pay to the Trustee of the New Haven Railroad the sum of $3.38 million on account of Penn Central Company's obligation in respect of the New Haven Railroad's share of excess income of the Grand Central Terminal Properties for the years 1967 and 1968 in cash by offset against adjustments calculated in the final postclosing adjustments pursuant to Section 7 of the agreement between the New Haven Trustees and the Pennsylvania Railroad Company and the New York Central Railroad Company dated April 21, 1966, as amended, as provided in the order of the reorganization court dated July 11, 1969;

D. That Penn Central Company shall deliver to the Trustee of the New Haven Railroad an instrument wherein Penn Central undertakes that unless the market price of Penn Central Company common stock reaches and maintains a price of $87.50 per share on the New York Stock Exchange for a period of five consecutive days on which the Exchange is open and doing business between the date of final consummation of the Plan of Reorganization of the New Haven Railroad and February 1, 1978, Penn Central Company shall on February 8, 1978 pay to the New Haven Railroad or its successor or successors, in cash,

the difference between the average of the means between the high and low prices of Penn Central Company common shares on the New York Stock Exchange for the 30 business days next preceding February 1, 1978 on which the Exchange is actually operating and there are sales of Penn Central shares of common stock and $87.50 for each of the 950,116 shares heretofore conveyed to the New Haven and for each of the shares of additional consideration ordered and decreed herein. The said instrument shall contain the following stipulations and such others as may be appropriate:

1. Penn Central Company may, at its option at any time between the date of final consummation of the Plan of Reorganization of the New Haven Railroad and February 1, 1978, discharge its obligation to pay the difference between such average market price and $87.50 by paying on one or more blocks of 50,000 shares to the New Haven Railroad, or its successor or successors, the difference between the mean market price for sale of Penn Central common stock and $87.50 per share as of a specific day of sales on the Exchange, which shall previously have been designated by Penn Central Company in a written notice delivered to the New Haven Railroad, or its successor or successors, at least five days prior to such market date;

2. The benefits of this undertaking shall inure only to the New Haven Railroad and its successor or successors, and do not follow the shares into the hands of a purchaser if they are sold. Distributees of the New Haven Railroad in the event of its liquidation shall be deemed to be successors. The New Haven Railroad's rights under this undertaking shall survive the sale of all or any part of the 950,116 shares or the additional shares required to be

delivered by this decree subject, however, to subparagraph 4 and 5 below. Nothing herein contained shall be construed as a limitation upon the right of the New Haven Railroad, or its successors, to sell or otherwise dispose of the Penn Central Company shares which it owns;

3. For purposes of the five-day test period herein specified, the market price of Penn Central share shall be deemed to have reached $87.50 per share if and only if the mean of the high and low quotations for the day is $87.50 or above; and such price shall be deemed to have been maintained if and only if the mean of the high and low quotations on the successive days is $87.50 or above;

4. Penn Central Company shall be discharged from its obligation to pay the difference between the 30-day average market price immediately preceding February 1, 1978, and $87.50 with respect to all Penn Central common shares sold by the New Haven Railroad or its successor prior to February 1, 1978, at a price of $87.50 or above (before deducting commissions, taxes and other expenses of sale); and

5. In the event that the New Haven Railroad or its successor sells Penn Central common shares prior to February 1, 1978, at a price less than $87.50 (before deducting commissions, taxes and other expenses of sale), but in excess of such 30-day average market price, Penn Central Company shall be credited with the dollar amount of such excess over such 30-day average market price in computing the amount of Penn Central's obligation to pay the difference between such 30-day average market price and $87.50.

The said instrument shall also contain appropriate provisions whereby the price of $87.50 and the market price of Penn Central shares, and the number of shares affected will be adjusted to reflect extraordinary transactions such as mergers, stock splits, and distribution of property on account of Penn Central shares other than normal dividends, and whereby any disputes in regard to the application of the instrument shall be determined by the reorganization court.

The parties are directed, upon this decree becoming final, to cooperate in the preparation of such an instrument; in the event of their inability to agree, the form of the instrument shall be determined by the reorganization court.

E. That in all other respects, the Commission's findings and conclusions as to matters contained in its Fourth Supplemental Report and Order are sustained.

Henry J. Friendly
United States Circuit Judge

Richard H. Levet
Senior United States District Judge

Dated: September 11, 1969.

Appendix of Constitutional Provisions and Statutes

Fifth Amendment to the United States Constitution

No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or naval forces, or in the Militia, when in actual service in time of War or public danger; nor shall any person be subject for the same offence to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property without due process of law; nor shall private property be taken for public use, without just compensation.

Section 5(2) of the Interstate Commerce Act (49 U.S.C. § 5(2))

(a) It shall be lawful, with the approval and authorization of the Commission, as provided in subdivision (b)—

(i) for two or more carriers to consolidate or merge their properties or franchises, or any part thereof, into one corporation for the ownership, management, and operation of the properties theretofore in separate ownership; or for any carrier, or two or more carriers jointly, to purchase, lease or contract to operate the properties, or any part thereof, of another; or for any carrier, or two or more carriers jointly, to acquire control of another through ownership of its stock or otherwise; or for a person which is not a carrier to acquire control of two or more carriers

through ownership of their stock or otherwise; or for a person which is not a carrier and which has control of one or more carriers to acquire control of another carrier through ownership of its stock or otherwise; or

(ii) for a carrier by railroad to acquire trackage rights over, or joint ownership in or joint use of, any railroad line or lines owned or operated by any other such carrier, and terminals incidental thereto.

(b) Whenever a transaction is proposed under subparagraph (a), the carrier or carriers or persons seeking authority therefor shall present an application to the Commission, and thereupon the Commission shall notify the Governor of each State in which any part of the properties of the carriers involved in the proposed transaction is situated, and also such carriers and the applicant or applicants (and, in case carriers by motor vehicle are involved, the persons specified in section 205 (e)), and shall afford reasonable opportunity for interested parties to be heard. If the Commission shall consider it necessary in order to determine whether the findings specified below may properly be made, it shall set said application for public hearing; and a public hearing shall be held in all cases where carriers by railroad are involved unless the Commission determines that a public hearing is not necessary in the public interest. If the Commission finds that, subject to such terms and conditions and such modifications as it shall find to be just and reasonable, the proposed transaction is within the scope of subparagraph (a) and will be consistent with the public interest, it shall enter an order approving and authorizing such transaction, upon the terms and conditions, and with the modifications, so found to be just and

reasonable: *Provided,* That if a carrier by railroad subject to this part, or any person which is controlled by such a carrier, or affiliated therewith within the meaning of paragraph (6), is an applicant in the case of any such proposed transaction involving a motor carrier, the Commission shall not enter such an order unless it finds that the transaction proposed will be consistent with the public interest and will enable such carrier to use service by motor vehicle to public advantage in its operations and will not unduly restrain competition.

(c) In passing upon any proposed transaction under the provisions of this paragraph (2), the Commission shall give weight to the following considerations, among others: (1) The effect of the proposed transaction upon adequate transportation service to the public; (2) the effect upon the public interest of the inclusion, or failure to include, other railroads in the territory involved in the proposed transaction; (3) the total fixed charges resulting from the proposed transaction; and (4) the interest of the carrier employees affected.

(d) The Commission shall have authority in the case of a proposed transaction under this paragraph (2) involving a railroad or railroads, as a prerequisite to its approval of the proposed transaction, to require, upon equitable terms, the inclusion of another railroad or other railroads in the territory involved, upon petition by such railroad or railroads requesting such inclusion, and upon a finding that such inclusion is consistent with the public interest.

(e) No transaction which contemplates a guaranty or assumption of payment of dividends or of fixed charges,

shall be approved by the Commission under this paragraph (2) except upon a specific finding by the Commission that such guaranty or assumption is not inconsistent with the public interest. No transaction shall be approved under this paragraph (2) which will result in an increase of total fixed charges, except upon a specific finding by the Commission that such increase would not be contrary to public interest.

(f) As a condition of its approval, under this paragraph (2), of any transaction involving a carrier or carriers by railroad subject to the provisions of this part, the Commission shall require a fair and equitable arrangement to protect the interests of the railroad employees affected. In its order of approval the Commission shall include terms and conditions providing that during the period of four years from the effective date of such order such transaction will not result in employees of the carrier or carriers by railroad affected by such order being in a worse position with respect to their employment, except that the protection afforded to any employee pursuant to this sentence shall not be required to continue for a longer period, following the effective date of such order, than the period during which such employee was in the employ of such carrier or carriers prior to the effective date of such order. Notwithstanding any other provisions of this Act, an agreement pertaining to the protection of the interests of said employees may hereafter be entered into by any carrier or carriers by railroad and the duly authorized representative or representatives of its or their employees.

Section 1(18) of the Interstate Commerce Act (49 U.S.C. § 1(18))

After ninety days after this paragraph takes effect no carrier by railroad subject to this part shall undertake the extension of its line of railroad, or the construction of a new line of railroad, or shall acquire or operate any line of railroad, or extension thereof, or shall engage in transportation under this part over or by means of such additional or extended line of railroad, unless and until there shall first have been obtained from the Commission a certificate that the present or future public convenience and necessity require or will require the construction, or operation, or construction and operation, of such additional or extended line of railroad, and no carrier by railroad subject to this part shall abandon all or any portion of a line of railroad, or the operation thereof, unless and until there shall first have been obtained from the Commission a certificate that the present or future public convenience and necessity permit of such abandonment. Nothing in this paragraph or in section 5 shall be considered to prohibit the making of contracts between carriers by railroad subject to this part, without the approval of the Commission, for the joint ownership or joint use of spur, industrial, team, switching, or side tracks.

Section 1(20) of the Interstate Commerce Act (49 U.S.C. § 1(20))

The Commission shall have power to issue such certificate as prayed for, or to refuse to issue it, or to issue it for a portion or portions of a line of railroad, or extension thereof, described in the application, or for the partial

exercise only of such right or privilege, and may attach to the issuance of the certificate such terms and conditions as in its judgment the public convenience and necessity may require. From and after issuance of such certificate, and not before, the carrier by railroad may, without securing approval other than such certificate, comply with the terms and conditions contained in or attached to the issuance of such certificate and proceed with the construction, operation, or abandonment covered thereby. Any construction, operation, or abandonment contrary to the provisions of this paragraph or of paragraph (18) or (19) of this section may be enjoined by any court of competent jurisdiction at the suit of the United States, the Commission, any commission or regulating body of the State or States affected, or any party in interest; and any carrier which, or any director, officer, receiver, operating trustee, lessee, agent, or person, acting for or employed by such carrier, who knowingly authorizes, consents to, or permits any violation of the provisions of this paragraph or of paragraph (18) of this section, shall upon conviction thereof be punished by a fine of not more than $5,000 or by imprisonment for not more than three years, or both.

Section 77(b) of the Bankruptcy Act
(11 U.S.C. § 205(b))

A plan of reorganization within the meaning of this section (1) shall include provisions modifying or altering the rights of creditors generally, or of any class of them, secured or unsecured, either through the issuance of new securities of any character or otherwise; (2) may include provisions modifying or altering the rights of stockholders generally, or of any class of them, either through the issu-

ance of new securities of any character, or otherwise; (3) may include, for the purpose of preserving such interests of creditors and stockholders as are not otherwise provided for, provisions for the issuance to any such creditor or stockholder of options or warrants to receive, or to subscribe for, securities of the reorganized company in such amounts and upon such terms and conditions as may be set forth in the plan; (4) shall provide for fixed charges (including fixed interest on funded debt, interest on unfunded debt, amortization of discount on funded debt, and rent for leased railroads) in such an amount that, after due consideration of the probable prospective earnings of the property in light of its earnings experience and all other relevant facts, there shall be adequate coverage of such fixed charges by the probable earnings available for the payment thereof; (5) shall provide adequate means for the execution of the plan, which may include the transfer of any interest in or control of all or any part of the property of the debtor to another corporation or corporations, the merger or consolidation of the debtor with another corporation or corporations, the retention of all or any part of the property by the debtor, the sale of all or any part of the property of the debtor either subject to or free from any lien at not less than a fair upset price, the distribution of all or any assets, or the proceeds derived from the sale thereof, among those having an interest therein, the satisfaction or modification of any liens, indentures, or other similar interests, the curing or waiver of defaults, the extension of maturity dates of outstanding securities, the reduction in principal and/or rate of interest and alteration of other terms of such securities, the amendment of the charter of the debtor, and/or the issuance of

securities of either the debtor or any such other corporation or corporations for cash, or in exchange for existing securities, or in satisfaction of claims or rights or for other appropriate purposes; and may deal with all or any part of the property of the debtor; may reject contracts of the debtor which are executory in whole or in part, including unexpired leases; and may include any other appropriate provisions not inconsistent with this section.

The adoption of an executory contract or unexpired lease by the trustee or trustees of a debtor shall not preclude a rejection of such contract or lease in a plan of reorganization approved hereunder, and any claim resulting from such rejection shall not have priority over any other claims against the debtor because such contract or lease had been previously adopted. The term "securities" shall include evidences of indebtedness either secured or unsecured, bonds, stock, certificates of beneficial interest therein, certificates of beneficial interest in property, options, and warrants to receive, or to subscribe for, securities. The term "stockholders" shall include the holders of voting-trust certificates. The term "creditors" shall include, for all purposes of this section all holders of claims of whatever character against the debtor or its property, whether or not such claims would otherwise constitute provable claims under this Act, including the holder of a claim under a contract executory in whole or in part including an unexpired lease.

The term "claims" includes debts, whether liquidated or unliquidated, securities (other than stock and option warrants to subscribe to stock), liens, or other interests of whatever character. For all purposes of this section unsecured claims, which would have been entitled to priority

if a receiver in equity of the property of the debtor had been appointed by a Federal court on the day of the approval of the petition, shall be entitled to such priority and the holders of such claims shall be treated as a separate class or classes of creditors. In case an executory contract or unexpired lease of property shall be rejected, or shall not have been adopted by a trustee appointed under this section, or shall have been rejected by a receiver in equity in a proceeding pending prior to the institution of a proceeding under this section, or shall be rejected by any plan, any person injured by such nonadoption or rejection shall for all purposes of this section be deemed to be a creditor of the debtor to the extent of the actual damage or injury determined in accordance with principles obtaining in equity proceedings. The provisions of section 60 of this Act shall apply to a proceeding under this section. For all purposes of this section any creditor or stockholder may act in person or by an attorney at law or by a duly authorized agent or committee subject to the provisions of subsection (p) hereof. The running of all statutes of limitation shall be suspended during the pendency of a proceeding under this section.

Section 77(d) of the Bankruptcy Act
(11 U.S.C. § 205(d))

The debtor, after a petition is filed as provided in subdivision (a) of this section, shall file a plan of reorganization within six months of the entry of the order by the judge approving the petition as properly filed, or if heretofore approved, then within six months or August 27,

1935, and not thereafter unless such time is extended by the judge from time to time for cause shown, no single extension at any one time to be for more than six months. Such plan shall also be filed with the Commission at the same time. Such plans may likewise be filed at any time before, or with the consent of the Commission during, the hearings hereinafter provided for, by the trustee or trustees, or by or on behalf of the creditors being not less than 10 per centum in amount of any class of creditors, or by or on behalf of any class of stockholders being not less than 10 per centum in amount of any such class, or with the consent of the Commission by any party in interest. After the filing of such a plan, the Commission, unless such plan shall be considered by it to be prima facie impracticable, shall, after due notice to all stockholders and creditors given in such manner as it shall determine, hold public hearings, at which opportunity shall be given to any interested party to be heard, and following which the Commission shall render a report and order in which it shall approve a plan, which may be different from any which has been proposed, that will in its opinion meet with the requirements of subdivisions (b) and (e) of this section, and will be compatible with the public interest; or it shall render a report and order in which it shall refuse to approve any plan. In such report the Commission shall state fully the reasons for its conclusions.

The Commission may thereafter, upon petition for good cause shown filed within sixty days of the date of its order, and upon further hearings if the Commission shall deem necessary, in a supplemental report and order modify any plan which it has approved, stating the reasons for such modification. The Commission, if it approves a plan, shall

thereupon certify the plan to the court together with a transcript of the proceedings before it and a copy of the report and order approving the plan. No plan shall be approved or confirmed by the judge in any proceeding under this section unless the plan shall first have been approved by the Commission and certified to the court.

Provisions of Section 77(e) of the Bankruptcy Act (11 U.S.C. § 205(e)).

Upon the certification of a plan by the Commission to the court, the court shall give due notice to all parties in interest of the time within which such parties may file with the court their objections to such plan, and such parties shall file, within such time as may be fixed in said notice, detailed and specific objections in writing to the plan and their claims for equitable treatment. The judge shall, after notice in such manner as he may determine to the debtor, its trustee or trustees, stockholders, creditors, and the Commission, hear all parties in interest in support of, and in opposition to, such objections to the plan and such claims for equitable treatment. After such hearing, and without any hearing if no objections are filed, the judge shall approve the plan if satisfied that: (1) It complies with the provisions of subdivision (b) of this section, is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders; (2) the approximate amounts

to be paid by the debtor, or by any corporation or corporations acquiring the debtor's assets, for expenses and fees incident to the reorganization, have been fully disclosed so far as they can be ascertained at the date of such hearing, are reasonable, are within such maximum limits as are fixed by the Commission, and are within such maximum limits to be subject to the approval of the judge; (3) the plan provides for the payment of all costs of administration and all other allowances made or to be made by the judge, except that allowances provided for in paragraph (12) of subdivision (c) of this section, may be paid in securities provided for in the plan if those entitled thereto will accept such payment, and the judge is given power to approve the same.

If the judge shall not approve the plan, he shall file an opinion, stating his conclusions and the reason therefor, and he shall enter an order in which he may either dismiss the proceedings, or in his discretion and on motion of any party in interest refer the proceedings back to the Commission for further action, in which event he shall transmit to the Commission a copy of any evidence received. If the proceedings are referred back to the Commission, it shall proceed to a reconsideration of the proceedings under the provisions of subdivision (d) of this section. If the judge shall approve the plan, he shall file an opinion, stating his conclusions and the reasons therefor, and enter an order to that effect, and shall send a certified copy of such opinion and order to the Commission. The plan shall then be submitted by the Commission to the creditors of each class whose claims have been filed and allowed in accordance with the requirements of subdivision (c) of this section, and to the stockholders of each class, and/or to the committees or other representatives thereof, for acceptance or

rejection, within such time as the Commission shall specify. . . .

* * *

If it shall be necessary to determine the value of any property for any purpose under this section, the Commission shall determine such value and certify the same to the court in its report on the plan. The value of any property used in railroad operation shall be determined on a basis which will give due consideration to the earning power of the property, past, present, and prospective, and all other relevant facts. In determining such value only such effect shall be given to the present cost of reproduction new and less depreciation and original cost of the property, and the actual investment therein, as may be required under the law of the land, in light of its earning power and all other relevant facts.

Second Supplemental Order

Finance Docket No. 21989, etc.

PENNSYLVANIA RAILROAD COMPANY—MERGER—
NEW YORK CENTRAL RAILROAD COMPANY, etc.

November 16, 1967

Investigation of the matters and things involved in these proceedings having been made, further hearings having been held, and the Commission on the date hereof having made and filed a second supplemental report containing its findings of fact and conclusions thereon, which report is made a part hereof:

It is ordered, That as a prerequisite to this Commission's approval of the transactions authorized in 327 I.C.C. 475, The Pennsylvania Railroad Company and The New York Central Railroad Company are authorized and directed to include The New York, New Haven and Hartford Railroad Company, and its affiliates and subsidiaries, including the New England Transportation Company, in their system in the manner and under the terms found equitable and conditions prescribed in the said second supplemental report;

It is further ordered, That as part of the terms and conditions of said inclusion the Trustees of The New York, New Haven and Hartford Railroad Company, The Pennsylvania Railroad Company, and The New York Central Railroad Company be, and they are hereby, directed to file with the Commission a loan agreement, an amend-

ment to their agreement dated April 21, 1966, as modified October 4, 1966, and an appropriate form of Trustees' certificate in accordance with the terms and conditions in the aforesaid second supplemental report of the Commission no later than 35 days from the date of service of this order;

It is further ordered, That, subject to the terms and conditions in the aforesaid second supplemental report applicable thereto, The Pennsylvania Railroad Company is authorized to issue to the Trustees of The New York, New Haven and Hartford Railroad Company in connection with acquisition of the assets of that railroad (a) 950,000 shares of its common stock of the par value of $10.00 per share, additional shares as may be made necessary by the purchase price adjustments and anti-dilution provisions referred to in said report, and (b) $23,000,000 principal amount of 25-year Divisional First Mortgage Bonds, and such larger principal amount of bonds as may result from operation of the purchase price adjustment provisions; and to assume obligation and liability in respect of equipment trust obligations guaranteed by The New York, New Haven and Hartford Railroad Company and described in the application in Finance Docket No. 24361, the bonds and certificates of contingent beneficial interest to be issued pursuant to the Boston and Providence Railroad Corporation plan of reorganization, as described in *Boston & P. R. Corp. Reorganization,* 327 I.C.C. 10, and any other securities hereafter issued, assumed, or guaranteed by the Trustees of The New York, New Haven and Hartford Railroad Company under section 20a of the Interstate Commerce Act prior to acquisition of the properties of The New York, New Haven and

Hartford Railroad Company by The Pennsylvania Railroad Company which the latter may be required to assume or guarantee pursuant to the terms of the aforesaid agreement;

It is further ordered, That The Pennsylvania Railroad Company shall report concerning the matters herein involved in conformity with the order of the Commission, Division 3, dated May 20, 1964, as amended, respecting applications filed under section 20a of the Interstate Commerce Act (49 CFR 156.6);

It is further ordered, That, except as herein authorized, said stock and bonds shall not be sold, pledged, repledged, or otherwise disposed of by The Pennsylvania Railroad Company unless or until so ordered or approved by this Commission;

It is further ordered, That, if the authorities herein granted are exercised, The Pennsylvania Railroad Company shall submit for the consideration of this Commission three copies of the journal entries required to record the transactions and confirm in writing to this Commission, immediately after consummating the transactions authorized in Finance Docket No. 21989, the effective date of such consummation;

It is further ordered, That nothing herein shall be construed to imply any guaranty or obligation as to said stock or bonds, or dividends thereon, on the part of the United States;

It is further ordered, That the petition of Oscar Gruss & Son filed March 20, 1967, be, and it is hereby, dismissed;

It is further ordered, That the terms for the sale of the assets of the New York, New Haven and Hartford Rail-

road Company, Debtor, to the Pennsylvania, New York Central Transportation Company, originally filed as the first step of the plan of the Trustees of the New York, New Haven and Hartford Railroad Company, Debtor, for reorganization of that carrier, as described in said report, be, and they are hereby, approved;

It is further ordered, That consummation of the merger of The New York Central Railroad Company into The Pennsylvania Railroad Company shall constitute an irrevocable assent of The Pennsylvania New York Central Transportation Company to enter into a loan arrangement with the Trustees of The New York, New Haven and Hartford Railroad Company in accordance with the terms and conditions required in the said second supplemental report;

It is further ordered, That this order shall take effect and be in force 35 days from and after the date of its service and the inclusion directed is to be accomplished within 90 days from the date transfer of the assets of The New York, New Haven and Hartford Railroad Company to the Pennsylvania New York Central Transportation Company, pursuant to the report herein;

And it is further ordered, That the jurisdiction of this Commission be, and it is hereby, retained for the purpose of making such further order or orders in these proceedings as may be necessary or appropriate, in addition to those orders under jurisdiction expressly retained in the prior reports and orders of the Commission and to those orders which may be issued under section 5(9) of the Interstate Commerce Act.

By the Commission.

H. NEIL GARSON
Secretary